BEAR STEARNS

Equity Research

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Airlines

Fear and Loathing on the Pension Front

Competitive and Legislative Uncertainties Abound

- **PENSION FUNDING DEFICITS DRIVE UP LIQUIDITY RISK.** We estimate the non-bankrupt U.S. network airlines' defined benefit (DB) pension plan funding shortfall at $14 billion, with plan benefit obligations of $35 billion and plan assets of just $21 billion. Combined with weak yields and high oil prices, the status quo on pension cash contributions could drive more legacy-cost airlines into Chapter 11.

- **FEARING LARGER CASH CONTRIBUTIONS.** We estimate aggregate pension cash contributions should rise just 3% in 2005, to $1.3 billion; however, 2006 contributions could rise another 113%, to $2.7 billion, barring a legislative remedy. Given the limitations of pension accounting/modeling and the uncertainty surrounding the year-end expiration of the Pension Funding Equity Act of 2004 (PFEA), we provide detailed sensitivity tests in this report.

- **LOATHING UNITED TERMINATIONS AND PFEA EXPIRATION.** We believe airline managements must abhor the idea of United Airlines terminating its DB pension plans and emerging from bankruptcy leaner, meaner, and free of billions in liabilities. Worry is also growing about the expiring PFEA, which currently allows for lower cash contributions via postponed deficit reduction contributions and a higher discount rate.

- **CAPITOL HILL: A CRITICAL FACTOR.** Congressional action (or inaction) in the next 12 months will play a key role in whether airlines contribute more than 40% of projected operating cash flow to employee pension plans in 2006. We see meaningful differences in pension-related risk and, in descending order, rank the carriers as follows: Delta, Northwest, Continental, AMR, and Alaska Air.

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All pricing is as of the market close on March 10, 2005, unless otherwise indicated.

Executive Summary

Lingering in the back of every airline CEO's mind is the following worst-case pension scenario:

United Airlines succeeds in terminating its defined benefit pension plans, ridding itself of billions in obligations and eventually emerging from Chapter 11 with unit costs within range of low-cost carriers (LCCs). Then, at year-end, the Pension Funding Equity Act expires without any follow-on legislative relief. Combined with the cash flow pressures from weak yields and high oil prices, the required cash contributions to pension plans take liquidity down to bankruptcy risk levels. At the same time, the cost of capital rises (or access to capital shuts down) because the capital markets view legacy airlines as having an even greater margin disadvantage versus a swath of the industry beyond just the LCCs, and, ultimately, it is much tougher to go on outside of Chapter 11, let alone begin the long, hard work of repairing over-leveraged, distressed balance sheets.

From an equity market perspective, such a scenario could be part of what the industry needs — no more life lines and another liquidity crunch, so that more costs are stripped out and/or consolidation takes place, essentially letting the natural forces of the free market work more efficiently. However, if history is any guide, legislators won't be able to resist stepping into the ring, and some additional measure of relief will be granted.

In this report, we examine pension and other post-employment benefit problems facing the U.S. airline industry, with detailed analysis of the following:

- **Pension Funding: An Awful Situation That Could Become Worse.** We examine pension funding deficits and required cash contributions, with breakdowns and comparisons of defined benefit, defined contribution, profit sharing, and health care costs.

- **The Sizable Valuation Implications of Pension Funding Deficits.** We test earnings, cash flow, and valuation sensitivity to changes in interest rates, market return assumptions, and unfunded liability capitalization.

- **Pension Plans in Limbo.** There is uncertainty about the fate of United Airlines' defined benefit pension plans and the expiration of the Pension Funding Equity Act at year-end.

- **Legal Ruminations.** We discuss current law, new legislative proposals, access to funding waivers, and the potential effect of all on cash flows.

- **Retiree Health Care: A Growing Problem.** We explore the potential health care funding crisis.

- **How Do the Airlines Stack Up?** We measure the meaningful differences between pension and OPEB (retiree health care obligations) costs, and their relationship to operating cash flow and unrestricted cash balances.

- **Company Pension Profiles.** We present pension summaries for Alaska Air, AMR, Continental, Delta, and Northwest, with comments on United Airlines and US Airways.

- **Pensions 101.** A fast tutorial on this complicated subject should help those in need of a primer.

- **Appendix.** In a series of exhibits, we focus on cash burn and oil sensitivity.

AN AWFUL SITUATION THAT COULD BECOME WORSE

Pension Contributions Should Represent 50% of 2005 Operating Cash Flow with Oil at $46, 78% with Oil at $50

We estimate that the legacy airlines have defined benefit pension plans that are underfunded to the tune of $14 billion ($35 billion in plan benefit obligations versus $21 billion in plan assets) and will require about $1.3 billion in cash contributions this year, or $1.79 per share on average (assuming UAL does not terminate its plans, the total could be $2 billion, or $3 per share). These contributions represent about 50% of our operating cash flow forecast and 13% of the combined unrestricted cash balances.

This appears awful, but matters could become much worse next year. In 2006, barring a new legislative remedy, we believe the required cash contributions could increase 113%, to $2.7 billion, representing 45% of operating cash flow and 36% of existing cash with oil at $40/bbl and 79% of operating cash flow and 47% of cash with oil at $50. (Absent a replacement of PFEA 2004, pension discounting next year would revert to the 30-year Treasury yield, current-year DRC [deficit reduction contribution] requirements would be due in full, and the DRC deferrals from 2004-05 would need to be repaid in the near term.)

With regard to aggregate noncash P&L pension expenses, the outlook is also troublesome, since we project $1.6 billion in expenses in 2005 for Alaska Air, AMR, Continental, Delta, and Northwest ($2.35 per share on average).

We Believe Delta and Northwest Have the Greatest Pension Risk

Our analysis suggests that pension-related risk among legacy carriers operating outside of Chapter 11 is as follows, in ascending order: Alaska Air, AMR, and Continental, with Northwest and Delta bringing up the rear. In Exhibit 1 below, we set out our estimates for each carrier's funding deficit, defined benefit contributions, and pension expenses. We look at the costs on a unit basis for easy comparison and consider the relationship of the cash contributions/expenses to operating cash flow, unrestricted cash balances, and net earnings.

All told, if yields don't improve and oil remains above $45/bbl, the lack of a legislative band-aid for the pension funding problem could drive at least one more legacy carrier into bankruptcy, in our opinion:

- **Delta.** Based on our cash burn analysis, with $50 oil, Delta will be down to $1.1 billion by the end of this year (below its critical $1.5 billion level); however, even if we assume the carrier sells Comair and ASA for as much as $500 million, $50/bbl oil and pension obligations (barring a legislative fix) will chew up that cash by second-half 2006.

- **Northwest.** Northwest's situation is also troubling. Although the carrier has a larger unrestricted cash balance than Delta, without debt refinancing and pension law change, $50 oil could bring the carrier down to a critical $1.1 billion by mid-

2006 (with an 80% debt refi assumption, the carrier could survive until 2008), based on our analysis.

- **Continental.** Continental is only slightly better off. We estimate the carrier will be down to $1.1 billion (its bankruptcy risk valuation level) by early 2008 if we assume 80% debt refi and $50 oil. If the carrier fails to get its tentative labor deals ratified and is unsuccessful in refinancing its principal debt maturities in 2005, then the carrier will reach a bankruptcy-risk cash level in second-half 2005, in our estimation.

- **AMR.** AMR looks considerably stronger. Not even including the potential value from AMR's subsidiaries (American Eagle and American Beacon), with oil at $50, no change in pension law, and no debt refinancing, the carrier has enough cash to remain above its critical $1.5 billion level until 2007. Assuming AMR can refinance 80% of its principal debt maturities, we believe the carrier has a several-year liquidity cushion.

- **Alaska Air Group.** By any measure, Alaska Air Group has substantially less liquidity and pension risk, and we rank the carrier at the top of the heap. Even without any debt refinancing, we believe Alaska Air Group is nearly cash flow neutral with $50/bbl oil.

For more detail, please see our company pension profile section beginning on page 29 and our oil sensitivity cash burn in Exhibits 31-38 in the Appendix.

Our estimates are based on a generic pension model, which is highly dependent on assumptions about year-end discount rates, annual market performance, and contribution levels. Actual company results may differ.

Exhibit 1. Pension Summary — Cash Impact ($ in millions, except per share data)

	ALK	AMR	CAL[1]	DAL[2]	NWAC	Total/	UAL[3]	US Air[4]	AAI	AWA	FRNT[5]	JBLU	LUV
Plan Type	DB/DC	DB/DC	DB/DC	DB/DC	DB Plan	Average	DB/DC	DB/DC	DC Plan	DC Plan	DC Plan	DC Plan	DC Plan
12/31/2004													
Plan Assets (GAAP)	607	7,335	1,281	6,842	5,425	21,490	6,961	1,749	NA	NA	NA	NA	NA
Plan Benefit Obligations (PBO) (GAAP)	910	10,022	2,863	12,140	9,245	35,180	13,117	2,748	NA	NA	NA	NA	NA
PBO Pension Overfunded (Underfunded)	(303)	(2,687)	(1,582)	(5,298)	(3,820)	(13,690)	(6,156)	(999)	NA	NA	NA	NA	NA
ABO Pension Overfunded (Underfunded)	(161)	(1,823)	(1,131)	(5,239)	(3,565)	(11,919)	(5,692)	(971)	NA	NA	NA	NA	NA
Post Retirement Obligations (APBO)	(76)	(3,152)	NA	(1,835)	(921)	(5,984)	(3,069)	(1,369)	NA	NA	4	NA	80
2004 Assumed Rate of Return on Plan Assets	8.00%	9.00%	9.00%	9.00%	9.50%	8.90%	9.00%	8.01%	NA	NA	NA	NA	NA
2004 Assumed Discount Rate for Obligations	5.75%	6.00%	5.75%	6.00%	5.90%	5.88%	6.25%	6.00%	NA	NA	NA	NA	NA
2004 Asset Allocation: Equity/Fixed Income (remainder=other)	71%/29%	52%/38%	66%/28%	50%/28%	74%/20%	63%/29%	60%/35%	50%/41%	NA	NA	NA	NA	NA
2005E Revenue	2,847	19,638	10,352	15,701	11,854	60,393	NA	NA	1,326	2,467	843	1,647	7,183
2005E Operating Cash Flow (Oil at $46/bbl Base Assumption)	302	1,089	307	454	333	2,485	NA	NA	19	-12	-6	135	864
2005E Operating Cash Flow (Oil at $50/bbl)	278	784	181	208	147	1,598	NA	NA	6	-54	-13	120	853
2006E Revenue	2,967	20,161	10,837	16,662	12,315	62,942	NA	NA	1,648	2,602	NA	2,226	7,828
2006E Operating Cash Flow (Oil at $40/bbl Base Assumption)	332	1,982	798	1,558	1,214	5,884	NA	NA	60	24	NA	197	998
2006E Operating Cash Flow (Oil at $50/bbl)	267	1,149	511	546	897	3,371	NA	NA	11	-48	NA	145	923
2004 GAAP PBO Funding Status	67%	73%	45%	56%	59%	61%	53%	64%	NA	NA	NA	NA	NA
2004 GAAP ABO Funding Status	79%	80%	53%	57%	60%	66%	55%	64%	NA	NA	NA	NA	NA
2004 ABO per 2004 FTEs	12,448	20,099	29,383	75,763	90,616	47,560	98,991	39,427	NA	NA	NA	NA	NA
2004E P&L DB Pension Expense[6]	78	427	293	549	444	1,791	500	66	NA	NA	NA	NA	NA
2005E P&L DB Pension Expense[6]	89	380	227	440	500	1,637	NA	NA	NA	NA	NA	NA	NA
2005E DB Pension CASM	0.34¢	0.20¢	0.26¢	0.28¢	0.53¢	0.29¢	NA	NA	NA	NA	NA	NA	NA
2005E After-Tax EPS Impact	(2.12)	(1.51)	(2.20)	(2.22)	(3.70)	(2.35)	NA	NA	NA	NA	NA	NA	NA
2004 DB Expense	78	427	293	549	444	1,791	693	66	NA	NA	NA	NA	NA
2004 Defined Contribution & Profit Sharing Expense	25	163	30	150	NA	368	40	186	9	11	5	19	200
2004 Retirement (Health Care) Costs	9	264	NA	76	98	447	364	105	NA	NA	1	NA	18
2004 DB CASM	0.31¢	0.23¢	0.35¢	0.38¢	0.49¢	0.34¢	0.48¢	0.12¢	NA	NA	NA	NA	NA
2004 DC & Profit Sharing CASM	0.10¢	0.09¢	0.04¢	0.10¢	NA	0.07¢	0.03¢	0.33¢	0.08¢	0.04¢	0.07¢	0.10¢	0.26¢
2004 OPEB CASM	0.04¢	0.14¢	NA	0.05¢	0.11¢	0.08¢	0.25¢	0.19¢	NA	NA	0.01¢	NA	0.02¢
2004 Total DB, DC, OPEB CASM	0.44¢	0.46¢	0.38¢	0.53¢	0.59¢	0.49¢	0.75¢	0.63¢	0.08¢	0.04¢	0.08¢	0.10¢	0.28¢
Unrestricted Cash Balance (12/31/04)	874	2,929	1,460	1,799	2,459	9,521	1,300	738	334	306	149	449	1,305
2004E DB Pension Cash Contributions[6]	49	467	0	455	253	1,224	127	29	NA	NA	NA	NA	NA
2005E DB Pension Cash Contributions[6]	58	310	192	275	420	1,255	NA	NA	NA	NA	NA	NA	NA
2006E DB Pension Cash Contributions[7] Plan Freeze and 20-Yr Amort.	4	45	44	202	133	429	NA	NA	NA	NA	NA	NA	NA
2006E DB Pension Cash Contributions[7] Bush Proposal (7-Yr Amort.)	71	314	288	726	704	2,103	NA	NA	NA	NA	NA	NA	NA
2006E DB Pension Cash Contributions[7] PFEA expires (5-Yr Amort.)	76	377	356	962	901	2,672	NA	NA	NA	NA	NA	NA	NA
2005E After-Tax Projected Pension Cash per Share Impact	(1.38)	(1.24)	(1.86)	(1.39)	(3.11)	(1.79)	NA	NA	NA	NA	NA	NA	NA
2005E Pension Cash Contribution to 4Q04 Cash Balance	7%	11%	13%	15%	17%	13.2%	NA	NA	NA	NA	NA	NA	NA
2005E Pension Cash Contribution to 2005E Op. Cash Flow	19%	28%	63%	61%	126%	50.5%	NA	NA	NA	NA	NA	NA	NA
2005E Pension Cash + Debt Mat.+ Net Capex to 2005E Op. Cash Flow	93%	159%	327%	310%	411%	233.3%							
2006E (20-Yr Amort.) Pension Cash Contribution to 2006E Op. Cash Flow	1%	2%	6%	13%	11%	7.3%	NA	NA	NA	NA	NA	NA	NA
2006E (7-Yr Amort.) Pension Cash Contribution to 2006E Op. Cash Flow	21%	16%	36%	47%	58%	35.7%	NA	NA	NA	NA	NA	NA	NA
2006E (5-Yr Amort.) Pension Cash Contribution to 2006E Op. Cash Flow	23%	19%	45%	62%	74%	45.4%	NA	NA	NA	NA	NA	NA	NA
2006E (20-Yr Amort.) Pension + Debt Mat. + Net Capex to '06E Op. Cash Flow	57%	80%	94%	94%	112%	90.7%	NA	NA	NA	NA	NA	NA	NA
2006E (7-Yr Amort.) Pension + Debt Mat. + Net Capex to '06E Op. Cash Flow	77%	93%	124%	128%	159%	119.2%	NA	NA	NA	NA	NA	NA	NA
2006E (5-Yr Amort.) Pension + Debt Mat. + Net Capex to '06E Op. Cash Flow	78%	97%	133%	143%	175%	128.9%	NA	NA	NA	NA	NA	NA	NA

DB = defined benefit pensions, where employer bears investment risk. DC = defined contribution pensions plan such as 401(k), where the employee assumes the investment risk. PBO = projected benefit obligation (assumes future wage inflation). ABO = accumulated benefit obligation (pension obligations already accrued; if a plan were frozen, this would be GAAP analogous amount). APBO = accumulated post retirement benefits obligation. OPEB includes post-employment health care benefits — medical, dental, vision, hearing, and other health-related benefits, whether provided separately or through the pension plan. Other benefits include life insurance, disability, long-term care, etc., when provided separately from a defined benefit pension plan. Operating cash flow = net income + D&A + pension expense; assumes no impact from change in net working capital.

(1) Continental's 2005E required pension contribution is $307 million; however, in the table above, which focuses on cash, we exclude $65 million in stock contributed in the first quarter and assume $50 million in savings from ratification of labor deals. Similarly, pension expense is $315 million, though it is expected to decline by $90 million upon ratification of tentative labor agreements.

(2) Delta froze its DB plan as of 12/31/04, eliminating future service accruals, though wage increases will still be factored into benefit calculations. 2004 pension expense excludes curtailment charges.

(3) UAL contributed $17 million and $110 million during the first and second quarters of 2004 ($700 million was estimated to be due last year), respectively, to its plans; however, the carrier currently does not expect to make any contributions to its pension plans before exiting from bankruptcy and intends to terminate its plans. UAL's information is as of 2003 except for cash.

(4) Effective February 1, 2005, the PBGC was appointed trustee of US Airways AFA, IAM, and CE plans. In 2004, prior to entering Chapter 11, the carrier had been obligated to contribute $155 million to its plan.

(5) FRNT is on a March fiscal year-end. FY2006 = 2005.

(6) Based on 2004 company 10k, third-quarter 2004 10Q data, fourth-quarter 2004 conference calls, company guidance, and Bear, Stearns & Co. Inc. estimates.

(7) Bear Stearns' forecasts: 2006 forecasted pension cash contributions assume expiration of the Pension Funding Equity Act of 2004. Three scenarios (assuming an even amortization repayment schedule): 1) assumes plan freezes and a 20-year DRC amortization, 2) assumes a seven-year DRC amortization (Bush proposal), and 3) assumes PFEA expires and a five-year DRC amortization.

Actual company results may vary considerably. Please see our September 2003 Airline Pension report for more information.

Note: Firms may be able to contribute limited amounts of stock in certain circumstances instead of cash. In addition, firms may apply for IRS waivers that could allow them to spread payments out over five or so years. Furthermore, interest rate changes, asset returns, and legislative changes could have significant impacts on these forecasts.

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance; First Call.

While ERISA and the Internal Revenue Code rules dictate funding periods ranging from as few as three to as many as 30 years, after surveying our companies and for purposes of this report, we assume for simplifying reasons that deficit reduction contributions are repaid in five years under current law and would continue to be due in this time frame should PFEA expire without replacement.

Should Investors Capitalize the Unfunded Portion of the Pension Liability?

Pension funding deficits pose some important valuation considerations. Should investors capitalize the unfunded portion of a company's pension liability, which would be tantamount to assuming it has to issue debt to fund its plans? This is not an easy decision, as interest rates, pension asset returns, and many other variables could reduce or even eliminate current funding deficits down the road.

As a tool for those who choose to book the funding shortfall, we provide our current EV/EBITDAR forecasts with and without the 2004 ABO funding gap in the context of the carriers' historical means. Not surprisingly, inclusion of pension deficits leads to more expensive valuations, with Northwest's and Delta's expanding by roughly 30% each.

Exhibit 2. Pension Deficit Could Affect Valuation

	2006E EV/EBITDAR			Historical EV/EBITDAR
	Without Pension	Incl. Pension	% Chg.	Without Pension
AMR	6.0x	6.6x	10%	5.2x
CAL	7.5x	8.1x	9%	5.6x
DAL	6.8x	8.7x	27%	4.6x
NWAC	5.6x	7.5x	34%	4.7x
ALK	4.9x	5.2x	6%	7.8x

Note: Only includes the 2004 ABO underfunding amount, assumes borrowed underfunded amount to make plan whole.
EV= equity market capitalization + total debt, incl. operating leases less unrestricted cash.

Source: Bear, Stearns & Co. Inc. estimates.

Valuation Sensitivity to Discount Rates and Market Return Assumptions

What are the implications for P/E, P/EBITDA, and EV/EBITDAR as discount rate and market return assumptions change? In the exhibit below, we isolate the EPS and P/E impact of a 50-basis-point (bp) change in the discount rate or the rate of return assumption used to measure pension plan expenses. All told, valuations could appear to be 3%-35% more expensive or 3%-21% cheaper thanks to a 0.5%-point change in the underlying pension expense input.

Exhibit 3. Valuation Sensitivity to Discount Rate Changes

	2006/7 P/E Sensitivity:								
		0.5% Change in the Pension Discount Rate				0.5% Change in the Assumed Rate of Return			
	No Change	-50 Bps	% Chg.	+50 Bps	% Chg.	-50 Bps	% Chg.	+50 Bps	% Chg.
AMR	8.5x	11.5x	33%	7.5x	-20%	9.4x	15%	7.2x	-12%
CAL	9.5x	12.5x	35%	7.5x	-21%	9.5x	6%	8.5x	-5%
DAL	4.5x	5.5x	22%	3.5x	-15%	4.7x	19%	3.4x	-14%
NWAC	6.5x	7.5x	31%	5.5x	-19%	6.6x	19%	4.8x	-14%
ALK	9.5x	9.5x	7%	8.5x	-6%	9.0x	3%	8.6x	-3%

Note: ALK, AMR, CAL, and NWAC are off of 2006 estimates. DAL assumes a hypothetical normalized 7% op. margin in 2007.

Source: Bear, Stearns & Co. Inc. estimates; company reports; First Call.

Stock Options Will Also Hit Valuations This Year

Per SFAS No. 123R, U.S. airlines will be required to expense stock options using a fair value method beginning in the third calendar quarter this year. As a result, we expect some valuation headwinds for the profitable segment of the industry that utilizes stock options to a greater extent than the legacy carriers. Our 2005 and 2006 EPS estimates already take into account option expense for the U.S. airlines in our coverage; however, we suspect that the First Call mean may not fully reflect fair value option expense at present. Therefore, all else equal, estimates may be susceptible to downward pressure as the Street begins to incorporate option expenses into its second-half 2005/full-year 2006 estimates.

Further, option expense has broader implications than just added labor expense and hence lower net income. For instance, JetBlue expects to book a higher tax rate this year (47% versus 40% in previous years) due to its heavy reliance on incentive stock options, which generally do not provide for corporate tax deductibility.

Exhibit 4. Beware! Stock Option Expense Should Affect Valuation this Year

Stock Options Expenses: SFAS 123R			2004		First Call 2006 Mean P/E	
	Co. Disclosed 2H05E		Per Share	$ Mil.	Assuming No Option Expense	Less Option Expense
AMR	undisclosed		$0.40	$64	NM	NM
CAL	$9-15mn	$0.13	$0.09	$6	12.9x	18.2x
DAL	"may be material"		$0.29	$38	NM	NM
NWAC	already expensed		already expensed		NM	NM
AAI			$0.03	$2	19.5x	19.5x
ALK	$2-3mn	$0.09	$0.17	$5	9.3x	9.9x
AWA	"material impact"		$0.16	$6	NM	NM
FRNT			$0.05	$2	NM	NM
JBLU	$11mn	$0.10	$0.17	$19	30.0x	45.0x
LUV	$20mn	$0.02	$0.08	$74	22.6x	24.2x

Note: Net of tax figures. FRNT is FY 2004.

Source: Company reports; Bear, Stearns & Co. Inc. estimates; First Call.

Pension Accounting in SEC Crosshairs

In October 2004, the SEC began an informal inquiry into the accounting assumptions used for pension plans. Northwest Airlines and five other large defined benefit plan sponsors were among those queried for internal information regarding their pension and other post-retirement plans. While the criteria for the SEC's selection remain unclear, a cursory observation suggests that the aggregate pension obligation relative to a company's market capitalization may have been one screen applied. At first blush, Northwest stands out because of its expected rate of return assumption, which has exceeded that of its peers and the S&P 500 average by 50-150 basis points (bps) over the past three years. Nevertheless, when we examine plan asset allocations (see Exhibit 5 below), we discover that Northwest is more heavily weighted to equities than its peers.

Exhibit 5. Pension Accounting (GAAP) Assumptions

	Actual Discount Rates					Actual Expected Rate of Return				
	2000	2001	2002	2003	2004	2000	2001	2002	2003	2004
ALK	7.50%	7.25%	6.75%	6.00%	5.75%	10.00%	10.00%	8.00%	8.00%	8.00%
AMR	7.75%	7.50%	6.75%	6.25%	6.00%	9.50%	9.50%	9.25%	9.00%	9.00%
CAL	8.00%	7.50%	6.75%	6.25%	5.75%	9.50%	9.50%	9.50%	9.00%	9.00%
DAL	8.25%	7.75%	6.75%	6.13%	6.00%	10.00%	10.00%	10.00%	9.00%	9.00%
NWAC	7.90%	7.50%	6.75%	6.25%	5.90%	10.50%	10.50%	10.50%	9.50%	9.50%
S&P 500 Average		7.12%	6.59%	6.07%	NA	NA	9.07%	8.86%	8.34%	NA

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Pension accounting has often been the subject of investor concern, since changes in assumptions and realized market rates can materially affect a company's P&L. However, all the red ink in the airline industry in recent years seems to suggest that carriers are hardly making aggressive assumptions in order to boost net profits. In addition, if the SEC inquiry results in any sort of corrective action, it should only be a

GAAP accounting issue, since the SEC does not oversee pension cash funding guidelines — the Department of Labor (through ERISA) and the IRS do.

Exhibit 6. Pension Plan Asset Allocation

	ALK	AMR	CAL	DAL	NWAC	UAIR	UAL
Total Equity	71%	52%	66%	50%	74%	50%	60%
Fixed Income	29%	38%	28%	28%	20%	41%	35%
Other: Private Equity, Real Estate, Etc.	NA	10%	6%	22%	7%	9%	5%
Total	100%	100%	100%	100%	100%	100%	100%

Note: ALK, AMR, CAL, DAL, NWAC, and UAIR as of 2004; UAL as of 2003.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

That said, should companies feel the need to reduce their expected rate of return assumptions as a result of the SEC's scrutiny, the income statement effect could be noticeable. For example, using our pension forecasting models, leaving all else equal, we estimate the expense impact could range from $3 million to $36 million, or $0.07-$0.20 per share, for each one-half-percentage-point (50-bp) decrease in the expected rate of return assumption used for GAAP pension accounting. For example, should Continental lower its expected rate of return assumption by 50 bps, we would expect a $7 million increase in costs, or a $0.07 per share negative impact.

Exhibit 7. Pension Expense and Pension Liability Sensitivity

	50-Basis-Point Decline in Assumptions:				
	ALK	AMR	CAL	DAL	NWAC
	Effect on P&L Pension Expense from Change in Expected Return Assumption				
(mns)	($3)	($36)	($7)	($35)	($27)
EPS	($0.09)	($0.14)	($0.07)	($0.18)	($0.20)
	Effect on P&L Pension Expense from Change in Discount Rate Assumption				
(mns)	($9)	($68)	($35)	($40)	($40)
EPS	($0.21)	($0.27)	($0.34)	($0.20)	($0.30)
	Effect on GAAP PBO Pension Liaibility				
(mns)	$55	$623	$256	$750	$700
% 2004 PBO	6%	6%	9%	6%	8%

Note: Assumes 36% tax rate.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

UAL/US AIR AND LEGISLATIVE UNCERTAINTY

Fear surrounding airline pension funding deficits is exacerbated by uncertainty about the fate of United Airlines' defined benefit pension plans and the expiration of the PFEA at year-end. United Airlines' DB plans are about $6 billion underfunded, and the carrier has about $4 billion in minimum cash contributions due through the end of the decade. In July 2004, the carrier began skipping its required cash contributions and is working toward terminating its pension plans this May. While the carrier announced it has four offers for $2-$2.5 billion in exit financing, our sense is that the delivery of those funds is predicated on a successful resolution of the pension matter. At the same time, investors are concerned about the expiration of the PFEA and the potential for increases in already onerous pension cash contributions.

While United works toward a May termination of its pension plans (US Airways terminated its plans in January), the nonbankrupt airlines painfully watch their progress and reiterate the mantra of labor parity to their own work groups. By the end of the second quarter, we expect to have a better idea about UAL's attempt to scuttle its plans, but legislative uncertainty could linger through the year and even up until April 15, 2006, the deadline for calendar 2006's first pension installment.

HOW DID IT GET SO BAD?

A Perfect Storm

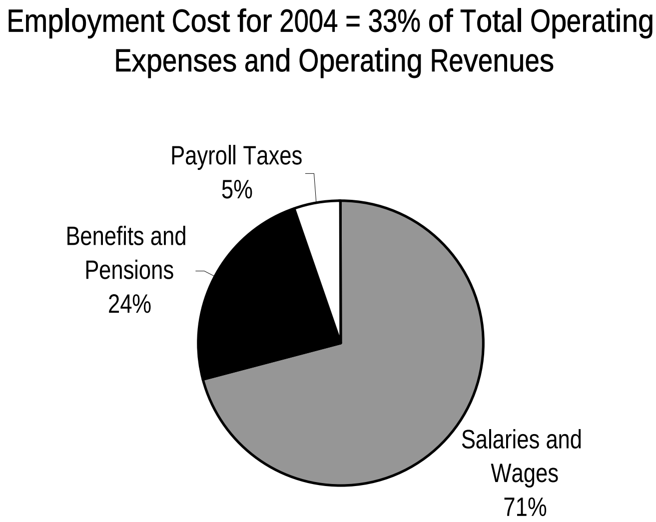
There are three major forces behind the airlines' pension problems:

- First, during the good times, the airlines negotiated generous packages with the unions — more than they can deliver through a full business cycle.

- Second, pension law effectively caps funding levels, which limits companies' ability to fortify plan assets during good years. (Despite running sizable funding deficits, many companies were not required to contribute much cash, if any, to their pensions prior to 2003.)

- Third, the combination of poor stock market performance and low interest rates helped to widen the gap between plan assets and liabilities. The market declines of 2000-02 shrank pension plan assets at the same time that lower interest rates boosted liabilities. (Lower interest rates increase the present value of projected benefit obligations [PBO] and poor market returns decrease the value of plan assets, while higher interest rates lower the present value of obligations and higher stock market returns increase the value of plan assets.)

Exhibit 8. Pension and Benefits Account for a Quarter of All Labor Costs



Note: Major and national passenger airlines for 12 months ended 3Q04.

Source: ATA.

What's more, despite positive asset returns in 2004, our 60%/40% pension fund proxy had pension assets up 8% (however, the average airline DB plan returned 12% last year), and interest rates finished down from 2003 levels, largely negating asset returns by increasing the present value of plan obligations and leaving pension plan funding levels right around last year's low water mark (see Exhibits 9 and 10 below). Hence, pension plans are still in dire straits. For example, Northwest mentioned that its plan assets rose more than 14% in 2004, yet its ABO shortfall was still $3.5 billion, up from $3.3 billion in 2003. Looking out to 2005 discount rates, due to the four-year weighted average calculation methodology, it is unclear how much rates might change by year-end even though more Fed rate hikes are coming down the pike.

Exhibit 9. Interest Rate Decline Could Offset Asset Gains in 2004

Interest Rates for Current Liability Funding Calculations		
Basis-Point Change from Previous Year-End		
12/31/2004	6.10%	***-0.45***
12/31/2003	6.55%	*-0.56*
12/31/2002	7.11%	*-0.23*
12/31/2001	7.34%	

2004 Proxy Pension Fund Return		
		Weighting
Lehman U.S. Bond Composite Index	4.5%	*40%*
S&P 500 Index Total Return	11%	*60%*
Aggregate Return	8.4%	

Note: Corporate bond weighted average interest rate as per the Pension Funding Equity Act of 2004. Lehman Allocation = 33% U.S. government, 33% investment grade corporates, 33% mortgages. The average airline DB plan returned 12% in 2004.

Source: Bear, Stearns & Co. Inc. estimates; Internal Revenue Service; Bloomberg.

Exhibit 10. Interest Rate Decline Could Offset Asset Gains in 2004

2004 Forecasted Market Return	2004E Incremental Funding Level Impact (in % points) Discount Rate for 2004: 6.0%	6.2%	6.4%	6.6%	6.8%	7.0%
1%	-6%	-4%	-2%	1%	3%	6%
4%	-5%	-2%	0%	2%	5%	8%
7%	-3%	-1%	2%	4%	7%	10%
10%	-1%	1%	3%	6%	9%	12%
13%	0%	3%	5%	8%	11%	14%
16%	2%	4%	7%	10%	13%	16%

Composite = ALK, AMR, CAL, DAL, NWAC.

Source: Bear, Stearns & Co. Inc. estimates.

In response to the looming year-end expiration of a temporary fix to funding rules, players in several corners have espoused remedies of both a short- and long-term nature. In early January, the Bush Administration unveiled a set of proposals to simplify and strengthen funding rules (shore up the federally insured pension funding system [PBGC]), including: 1) higher premiums, 2) duration-matched discount rates, 3) risk-based liability measures, and 4) more leverage for the PBGC in the Chapter 11 process. ALPA, the largest pilots union, as well as Northwest Airlines CEO Douglas Steenland, have called for freezing DB plans and much longer amortization periods for making up funding shortfalls (versus today's often much shorter time frame).

While ERISA and the Internal Revenue Code rules dictate funding periods ranging from as few as three to as many as 30 years, after surveying our companies and for purposes of this report, we assume for simplifying reasons that deficit reduction contributions are repaid in five years under current law and would continue to be due in this time frame should PFEA expire without replacement.

For its part, Congress could proffer its own set of measures and/or embrace the Administration's proposals to one degree or another. Rep. John Boehner (R-Ohio) is expected to continue the charge for pension reform in the House this term. In the Senate, Finance Committee Chair Chuck Grassley (R-Iowa) has already reintroduced pension legislation. While we applaud moves to freeze DB plan liabilities, we note that the trend to offer generous replacement DC plans can be just as costly, if not more so, in terms of current pension expenses and contributions.

CURRENT LAW TO EXPIRE IN 2005

The Pension Funding Equity Act (PFEA) of 2004

The PFEA, signed into law in April 2004, provided for significant deficit reduction contribution deferrals, which are ERISA-mandated accelerated pension funding requirements. The airlines received an 80% DRC reprieve in 2004 and 60% this year. In addition, the law changed the discount rate benchmark used to determine normal contributions from the 30-year Treasury to a 20-plus-year high-grade corporate bond series (AAA, AA, A). (A rise in the discount rate has the effect of lowering the present value of future liabilities, in turn reducing annual cash funding requirements.) We believe that the combined effect of switching to a corporate bond discount rate and an 80% deferral saved the airlines an estimated $1 billion in cash last year.

This year, despite the 60% DRC deferral and higher discount rate, the carriers ex UAL will still need to fund $1.3 billion in pension contributions, up from $1.2 billion in 2004, or 50% of our estimated operating cash flow for the group. Absent a replacement of PFEA 2004, pension discounting next year would revert to the 30-year Treasury yield, the current-year DRC requirements would be due in full, and the DRC deferrals from 2004-05 could become due in as short as three to five years. All of this could set the stage for a massive cash crunch in the next year or two unless oil prices crater and yields suddenly rebound.

Legislative Proposals

Bush Administration Proposes Pension Overhaul, But Not Enough to Spare Airlines

On January 10, Secretary of Labor Elaine Chao outlined the Bush Administration's pension reform initiatives. In our view, the salient issues for airline pensions in the President's proposal are: 1) higher standard premiums (from $19 per participant up to $30), plus additional risk-based premiums for severely underfunded plans; 2) seven-year amortization periods for making up unfunded liabilities versus today's potentially shorter time frame; 3) duration-matching yield curves for liability discounting; 4) requiring financially-weak sponsors to use a more conservative funding measure; 5) empowering the PBGC to perfect liens in bankruptcy proceedings; 6) disallowing lump-sum distributions at severely underfunded plans; and 7) freezing PBGC guarantee levels once a sponsor enters bankruptcy.

Exhibit 11. Administration's Proposals Seen as Largely Negative for Airlines

	Impact on Airlines	Notes
DRC Amortization (7 years)	Positive	Better than today's 3-5 year minimum
Duration-matched discount rate	Unclear	Plans with durations over 23 years could benefit
At-Risk Liability Measure	Negative	Non-investment grade likely = higher liabilites = higher DRC payments
Increase in Flat-Rate Premiums	Negative	Would increase to $30 from $19 per participant
Change in Variable-Rate Premiums	Unclear/Negative	Today, $9 per $1,000 of underfunding vs. weak financial sponsors' pay based on at-risk liability
PBGC Lien Perfection in Ch. 11	Negative	Could reduce assets available for other creditors

Note: U.S. legacy carriers are rated non-investment grade by the major credit agencies as of February 2005.

Source: Bear, Stearns & Co. Inc. estimates.

While the full potential effect of enacting the Administration's proposals is uncertain at this time, our initial take is that the airlines would see little benefit, and could perhaps suffer even more financial pressure under the Bush plan. For example, under the Bush proposal, the seven-year amortization period would likely leave carriers such as Delta and Northwest (and UAL, if does not succeed in terminating its plans in Chapter 11) with hefty pension cash obligations each year. Similarly, requiring duration matching could in fact enervate funding levels, depending on plan duration levels. For example, a plan with a duration under 23 years as of December 2004 would have used a lower rate than the current corporate bond rate had the Administration's plan been in effect at the time.

Further, other provisions, such as higher premiums, PBGC superpriority in bankruptcy proceedings, and prohibition of lump-sum payouts at deeply underfunded plans should strengthen plans; however, should early retirement-eligible employees fear enactment of the anti-lump sum payout provision, a cascade of early retirements could ensue, similar to what occurred at Delta last year, which could serve to weaken a sponsor's financial position.

Exhibit 12. Administration's Seven-Year Amortization Offers Scant Relief and Would Need to Double to Provide Meaningful Cash Flow Assistance

Illustration of DRC Burden: Hypothetical Amortization Schedules (per year contribution)

	ALK	AMR	CAL	DAL	NWAC	UAL
ABO Shortfall	(161)	(1,823)	(1,131)	(5,239)	(3,565)	(5,692)
5 Years 2006-2010	(17)	(181)	(178)	(806)	(533)	(885)
7 Years 2006-2012 (Bush proposal)	(12)	(130)	(127)	(576)	(381)	(632)
15 Years 2006-2020	(6)	(60)	(59)	(269)	(178)	(295)
20 Years 2006-2025	(4)	(45)	(44)	(202)	(133)	(221)
25 Years 2006-2030	(3)	(36)	(36)	(161)	(107)	(177)

Note: Assumes 2004 ABO shortfall is equal to 2004 current liability funding level and funding level rises to 90% over stated period. 2004 likely reduced funding gaps a touch as assets rose, offset by declining interest rates. CAL has reached tentative labor agreements, which, if ratified, could freeze its DB plans and significantly lower pension funding requirements. UAL figures use 2003 ABO.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Airline employees have also taken a less-than-favorable view of the Administration's plan, as evidenced by United's pilot union chief, Mark Bathurst, who remarked that "taken as a whole, [the Bush proposal] would make it much more costly for United to maintain its current pension plans." Nor is it just the unions — Scott Yohe, Delta's senior vice president of government affairs, declared, "The Administration's proposal would not help us. The primary reason is not the seven years, but the interest rate assumption, which would not give us the kind of relief we are looking for in terms of the funding obligations we have got in the near term."

Northwest Airlines CEO and ALPA President Make Proposal

One of the more outspoken airline executives on pension issues has been Northwest's CEO, Douglas Steenland. Along with Duane Woerth, president of ALPA and a former PBGC director, Northwest's chief penned a *Wall Street Journal* article espousing a three-phase process:

- First, companies and their unions would agree to freeze the existing defined benefit plan accruals (i.e., no further benefit accruals would be allowed).

- Next, concurrent with the defined benefit freeze, the parties would establish a replacement defined contribution plan. While a replacement plan would likely be partially company funded, the investment performance risk rests with the employees.

- Last, Congress would need to amend ERISA to permit plan sponsors to meet their DRC requirements over a much longer time period than today's potentially shorter time frame (e.g., three to five years).

The first two steps can be accomplished by the companies under existing law, as evidenced by Delta's November 2004 pilot contract and Continental's recent tentative agreements. However, the ultimate success of such a move, from a cash flow perspective, appears to rest on the extension of DRC amortizations.

Senate Finance Bill Reintroduced: NESTEG (S.219)

On January 31, 2005, Senate Finance Committee Chairman Chuck Grassley and ranking member Max Baucus reintroduced their pension reform legislation from last year, titled The National Employee Savings and Trust Equity Guarantee (NESTEG) Act. For airlines, the main thrust of NESTEG is replacing the 30-year Treasury Bond-based discount rate with a corporate bond-based yield curve. As we mentioned earlier in regard to the Administration's proposal, depending upon the duration of a given pension plan, a switch to a yield curve could adversely affect plan sponsors by raising liabilities and, in turn, plan expenses. For example, at a Senate Finance Committee hearing on March 1, 2005, witnesses from The Business Roundtable noted that the Administration's yield curve proposal could "increase pension liabilities for a typical mature plan by 10% or more. In some cases, the immediate liability increase could be even greater. For large plans, this could cost billions of dollars."

FUNDING WAIVERS — ADMINISTRATIVE RELIEF

In times of duress, airlines can petition federal administrative agencies for pension funding waivers. The Department of Labor's (DOL) Employee Benefits Security Administration has the authority to allow exemptions to certain ERISA rules, such as contributions of in-kind securities to a DB plan. For its part, the IRS has the authority to grant waivers deferring current contribution requirements to the following year. Northwest Airlines was a beneficiary of these agencies' administrative power in 2003, when the IRS permitted it to defer $454 million in 2003 minimum funding requirements. Funding waivers are limited to three in 15 years, and repayments are generally made over a five-year period. In return for this deferral, Northwest's plans received liens on some Northwest planes, landing slots, and routes.

Similarly, the DOL emphasized that its decision to exempt additional firms would be made on an individualized basis after a thorough review of each situation. However, in order to obtain a waiver, a sponsor must demonstrate that it is experiencing *temporary* hardship, and given the current state of the industry, it may be more challenging to convince the government of such a transitory misfortune. As United highlighted in its court filings (see exhibit below), the medium-term effect of a waiver is likely to only enlarge cash funding needs, as sponsors are required to repay the waived amount plus interest to the plan generally over five years.

Exhibit 13. Waivers Only Delay Funding Temporarily, Leading to Increased Total Contributions
($ in billions)

United Airlines Minimum DB Funding Contributions		
	No Waiver	Waiver
2005E	$1.2	$0.2
2006E	$1.0	$0.4
2007E	$1.5	$1.0
2008E	$0.6	$1.4
2009E	$0.1	$1.2
2010E	$0.0	$0.5
Total	$4.4	$4.8

Source: United Airlines.

Exhibit 14. Waivers Remain a Possible Near-Term Funding Alternative: 2006-08?

IRS Waivers Remaining	
(sponsors permitted to 3 per 15 year period for each plan, spreads payment out over 5 years)	
ALK	3
AMR	3
CAL	3
DAL	3
NWAC	2 or 3
UAL	3

Note: NWAC used one waiver in 2003 for its contract and salaried plans, leaving two for those plans and three for other plans.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Nevertheless, we would not be surprised if most carriers applied for IRS waivers for 2006 plan-year contributions, especially if Congress is slow to enact replacement legislation for PFEA 2004.

NONCASH CONTRIBUTIONS

In-kind contributions are another avenue available for satisfying some contribution needs, though they may require DOL approval. For example, in 2003, the DOL authorized Northwest to contribute stock in its then-privately held subsidiary, Pinnacle, to its DB plans in lieu of cash to satisfy its $223 million of 2002 funding requirements. Our sense is that the DOL is leery of allowing illiquid, noncash asset contributions to meet funding requirements.

AMR possesses several assets that it could monetize to meet some of its pension funding needs. For example, sole ownership of American Beacon Advisors, a money manager (with $37 billion in assets under management as of January 2005), could provide a decent cash boost. As a reference, see Exhibit 15 below, which illustrates potential values for asset management firms based on assets under management. It is difficult to home in on the true value of American Beacon Advisors as more than 50% of the assets are related to AMR, while a similar percentage is also managed by third parties, suggesting lower margins for the company as opposed to actively managed in-house funds. In addition, AMR could spin off its regional affiliate, American Eagle, which it also owns outright, similar to what its legacy peers Continental and Northwest did in 2002-03 with their regional entities. (See Exhibit 16 below for theoretical regional affiliate values based on publicly available revenue and market values for publicly traded peers.)

Exhibit 15. Hypothetical Values for Asset Management Firms

		Assets Under Management (AUM) (US$ in billions)			
		$15	$20	$25	$30
		Implied Value of Asset Management Unit (US$ in millions)			
Price to AUM Ratio	1.5%	$225	$300	$375	$450
	2.0%	$300	$400	$500	$600
	2.5%	$375	$500	$625	$750
	3.0%	$450	$600	$750	$900
	3.5%	$525	$700	$875	$1,050
	4.0%	$600	$800	$1,000	$1,200

American Beacon Advisors directly managed or served as fiduciary or financial advisor for $37.6 billion in assets at 1/31/05 consisting of $17.3 billion under active management and $20.3 billion as named fiduciary or financial adviser.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Exhibit 16. Regional Units Could Potentially Help Fund Pension Plans

Parent (former)	CAL	NWAC	AMR		DAL	
	XJT	PNCL	Eagle + Exec.	SKYW	ASA + Comair	Mean
ASMs (billions)	4.77	2.22	4.54	1.70	8.59	
Revenue (millions)	$1,461	$581	$1,820	$1,067	$2,117	
EBT Margin Actual (Assumed)	13%	11%	6%	12%	6%	12%
P/E Actual (Assumed)	6.6x	4.2x	7.1x	10.4x	7.1x	7.1x
Actual (Implied) Market Cap.	$604	$223	$496	$1,012	$577	
Assuming 12% EBT Margin			$988		$1,149	
10% of 2003 DB Plan Assets = Potential Contribution Ceiling			$734		$684	

Note: Second-half 2004 Scheduled ASMs from OAG via BACK Aviation; Revenue = 12 months ended 9/30/04. Comair and ASA revenues 12 months ended 6/30/04 using OD1A data. Market capitalization for XJT, PNCL, and SKYW as of 3/10/05. As reference, NWAC contributed $350 million (roughly 7% of total GAAP plan assets at 12/03) worth of privately held Pinnacle shares to its defined benefit plans in 2003. CAL contributed $100 million of XJT to its DB plans (approximately 8% of GAAP plan assets at 12/03), which was freely tradable. DAL paid over $2 billion for Comair and ASA according to media reports. Assumes 36% tax rate for wholly owned subsidiary implied market value calculations.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Ins and Outs of Noncash Contributions

Publicly traded securities — such as those of a sponsor's own equity, an affiliate, or other marketable securities — do not require a special exemption from the DOL, as was the case in Northwest's contribution in 2003. However, limitations still exist. For instance, the pension fund cannot own more than 25% of the entire equity, at least 50% of the equity must be in hands of shareholders unaffiliated with the parent company, and no more than 10% of plan assets may be invested in employer (and subsidiary) stock. That said, Continental contributed shares in former subsidiary ExpressJet in 2003 and did so again in January 2005 to mitigate the pension cash outflow. While recognizing the strategic value of regional subsidiaries, Delta CEO Gerald Grinstein acknowledged on December 15, 2004 that "you do not have to own them to get all of the benefits."

As in Northwest's case, companies may also try to obtain a DOL exemption that permits them to contribute prohibited transactions (illiquid, nontradable assets). For instance, U.S. Steel was permitted to contribute timber rights to its pension plans in 2003. However, a sponsor that proposes using a cashless asset with no ready market would need to supply an appraisal of the asset's worth, as well as convince the DOL that the assets could not be liquidated and that the pension plan would undertake no undue risk by accepting those assets (Northwest gave its pension plan put options so that it could put the Pinnacle stock back to Northwest at a given price).

FREEZING DB PLANS A LA DELTA PROVIDES LITTLE HELP FOR FUNDING LEVELS

Delta Air Lines' latest pilot deal, signed in November 2004, provided for a freeze of the pilots' defined benefit plans as of December 31, 2004, eliminating future service accruals; however, future wage increases will still get factored into pilots' final pension obligations. As a result of the partial freeze, Delta's DB liabilities should only grow due to salary inflation and interest accretion. Underscoring the uncertain future of airline DB benefits, on February 11, 2005, Northwest's pilot union leadership resolved to explore the possibility of freezing its plan to better protect its long-term viability. Momentum for plan freezes has seemingly picked up, as Continental disclosed that its recent tentative labor agreements contain some defined benefit plan freezes. While freezing a plan is most certainly more palatable for labor than termination, we believe that freezes do not go far enough to shore up cash flow needs and would still leave carriers that implement them at massive disadvantages to others that *do* terminate their plans.

UAL acknowledged in court filings (September 2004) that freezing its plans as of December 31, 2004 would only reduce its total cash outlay through 2008 by $875 million, leaving total cash contribution needs at $3.2 billion, a still-hefty sum that could certainly crimp liquidity. What's more, the estimated savings *exclude* the costs associated with any replacement plans that would most likely be established (north of $100 million per year). Recent history suggests some sort of company contributory defined contribution plan (some carriers' plans only match employees' contributions to a certain extent, while other plans contribute a specified amount of a person's salary). In addition, cash contribution needs are still driven by asset returns (the average return assumption was 8%-9%) and interest rates.

Furthermore, we examined carriers' PBO and ABO funding levels to get a sense of the potential funding level benefit should carriers freeze the salary inflation portion of their DB plans. For most of the carriers (see Exhibit 1), we found an average five-percentage-point improvement in 2004 funding levels (from 61% funded to 66% funded), which, in our view, underscores the limited improvement in funding levels (which determine cash funding needs) likely to be derived from the DB plan freeze in the near term.

PLAN TERMINATIONS

While three types of plan terminations exist under current law (distress, involuntary, and standard), for all intents and purposes, only the former two are relevant to the airline industry.

First of all, a standard termination requires a plan sponsor (in this case, an airline) to fully fund its plans either through lump-sum payouts or the purchase of annuities sufficient to satisfy all of its liabilities. In light of the substantial funding deficits (totaling $14 billion at Alaska Air, AMR, Continental, Delta, and Northwest) and the likely high cost required to acquire annuities, this form of termination appears to be out of reach.

Second, involuntary terminations arise when the PBGC itself terminates a pension plan after it reaches a certain level of distress (inability to make current payments to retirees, etc.), which would be a dream come true for plan sponsors, though the sponsor (and its equity) would likely find itself in a terminal condition before the PBGC would step in (e.g., PBGC taking over pension plans for United's pilots and ground workers). Distressed terminations, on the other hand, require carriers to demonstrate to the PBGC their inability to continue operations without abrogating their pension plans (to pass the distress test, a bankrupt sponsor may try to prove that "unless the plan is terminated [the plan sponsor], will be unable to pay all its debts pursuant to a plan of reorganization and will be unable to continue in business outside the chapter 11 reorganization process.").

In addition, since airline pension plans are part and parcel of collective bargaining agreements, union consent is needed unless a bankruptcy judge nullifies the contract, all of which suggests that a distress termination outside of Chapter 11 is highly unlikely.

ANOTHER DRAIN ON THE CARRIERS' COFFERS

While smaller in size than defined benefit pension obligations, another percolating benefit cost/liability problem for legacy airlines is retiree health care obligations. We estimate aggregate retiree health care obligations will be $726 million this year. While ERISA requires that pension plans meet established funding levels, retiree health care plans lack any similar funding requirement. For that reason, most carriers also have substantial unfunded accumulated post-retirement benefit obligations.

For example, 4% was the highest funding level among the legacy carriers with retiree health care (OPEB) obligations shown below at year-end 2004. As a result, retiree funding needs are met almost entirely from the corporate balance sheet and operating cash flow (as opposed to plan assets set aside, as in the case of pension plans). In addition, health care costs have been growing at a steady clip (up 8% in 2004) and are expected to rise an additional 6.6% this year, according to the bellwether Mercer survey. Some carriers began limiting their OPEB exposure several years ago by capping annual benefits. Nevertheless, the obligations loom large.

Based on the latest data available, AMR, Delta, and UAL each anticipated $190-$235 million in annual retiree health care funding needs through 2008. Given the meaningful sums of cash that these benefits divert from a carrier's coffers and the moves at UAL and US Airways in bankruptcy to streamline these expenses, we suspect that the other carriers will need to address these issues in the short to medium term.

Without ERISA funding guidelines, this is a pay-as-you-go scheme that could run into trouble as companies shrink and retirees' population rise. In addition to the carriers shown below, both Alaska and Frontier offer OPEB, although future payment forecasts are unavailable at this time (for historical information, see Exhibit 1). Further, Continental Airlines disclosed that its recent tentative labor agreements provide for some medical benefits to "eligible retirees" until they are eligible for Medicare, an apparent departure of past practice, wherein, unlike its legacy peers, the carrier did not offer retiree medical benefits (though this likely made the DB freeze more palatable for labor). As a result of offering retiree medical coverage, Continental expects to record $25 million in expenses in 2005 related to this plan.

Exhibit 17. Retiree Health Care (OPEB) Funding Liabilities and Plan Payout Forecast

	AMR	Delta	Northwest	US Airways	UAL	LUV
		Postretirement Benefit Payments from Plan Assets and Current Assets				
2005	$193	$188	$45	$63	$225	$2
2006	$187	$189	$48	$66	$235	$3
2007	$195	$191	$52	$71	$230	$5
2008	$201	$171	$55	$75	$235	$7
2009	$208	$163	$60	$74	$235	$9
2010 to 2014	$1,119	$669	$360	$421	$1,152	$78
Total - 2014	$2,103	$1,571	$620	$770	$2,312	$104
2004 APBO Unfunded Liability ($ mns)	($3,152)	($1,835)	($921)	($1,369)	($3,069)	($80)
2004 APBO Funded Status (%)	4%	0%	1%	0%	4%	0%
2004 P&L Expense	$264	$76	$98	$105	$364	$18
2004 P&L Expense per Share	$1.05	$0.38	$0.73	$1.23	$2.05	$0.01
2004 OPEB CASM	0.14¢	0.05¢	0.11¢	0.19¢	0.25¢	0.02¢
2005E Payment as % of 4Q Cash Balance	7%	10%	2%	NA	NA	0%
2005E Payment as % of '05 Op. Cash Flow	18%	41%	14%	NA	NA	0%
2005E Payment as % of '05 Pension Contribution	62%	68%	11%	NA	NA	NA

Note: UAL's information is as of 2003. In addition, the payment schedule is through 2004-08 and 2009-13.
OPEB includes post-employment health care benefits: medical, dental, vision, hearing, and other health-related benefits whether provided separately or through the pension plan; other benefits: life insurance, disability, long-term care, etc., when provided separately from a defined benefit pension plan. APBO = accumulated postretirement benefit obligation. Assumes 36% tax rate for 2004 expense per share.

Source: Bear, Stearns & Co. Inc.; company filings.

WE FIND MEANINGFUL DIFFERENCES BETWEEN PENSION AND OPEB COSTS

Last year, all the carriers in our coverage satisfied their required pension contributions. Nevertheless, the latest company guidance suggests hefty sums will be required in 2005, with Northwest leading the pack with $420 million in contributions. AMR, Delta, and Continental are not far behind with $310 million, $275 million, and $192 million (helped by a $65 million contribution in stock in January 2005 and its tentative labor agreements), respectively, in projected pension funding requirements in 2005, while Alaska should contribute close to $60 million.

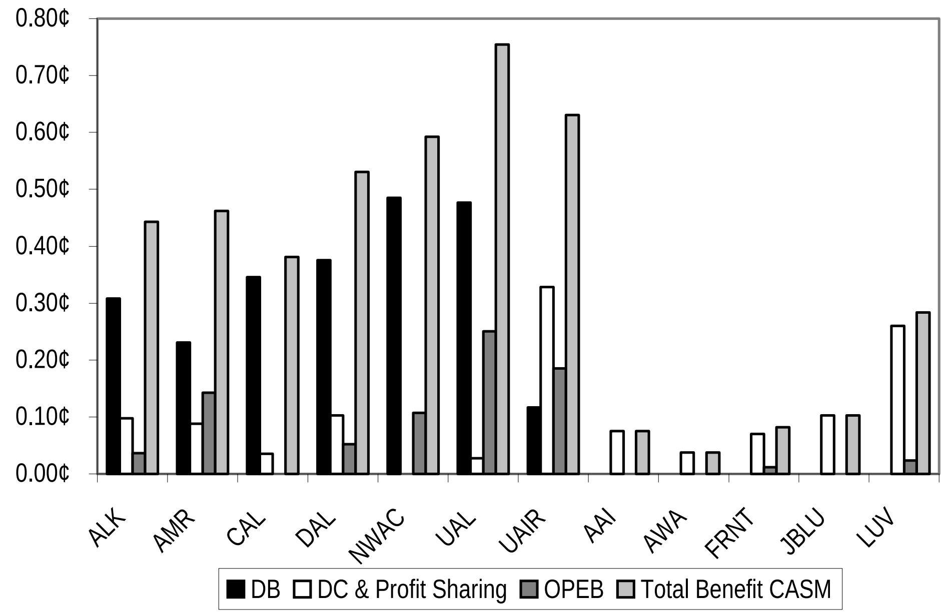
We believe that these contribution requirements should be considered in light of operating cash flow and other potential cash uses, such as debt maturities and unfinanced capital expenditures. Viewed in this way, we see that pension cash contributions will eat up a substantial portion of operating cash flow in 2005 (an aggregate 50%) and also represent a meaningful percentage of most carriers' unrestricted cash balances, 13% in total.

Based on our current 2005 estimates, Alaska appears to have the lowest pension cash contribution-to-operating-cash-flow ratio (19%) as well as the best pension cash-to-unrestricted cash balance ratio (7%). Northwest Airlines, on the other hand, has both the highest pension cash contribution-to-operating cash flow ratio (126%) and a pension contribution-to-cash balance ratio of 17%. Overall, we expect airlines to have an average $1.79 per share cash drag in 2005 due to DB pensions, representing 50% of their estimated 2005 operating cash flow and 5%-45% of their recent share prices. As we detail below, it could get much worse in 2006.

Pension, 401(k), Profit Sharing, and Retiree Health Approach $0.01 of CASM at Some Carriers

In the exhibit below, we depict the components of non-salary labor unit costs. For some airlines, these non-wage benefits amount to close to $0.01 of cost per available seat mile (CASM). Nevertheless, we also note that for LCCs such as Southwest and JetBlue, which utilize defined contribution and profit-sharing schemes, their respective non-salary labor CASM approximates the legacies' DB CASM. Put another way, replacing DB plans with healthy DC and profit-sharing programs may not be the answer to the near-term cash crunch, though the longer-term benefits are less disputable.

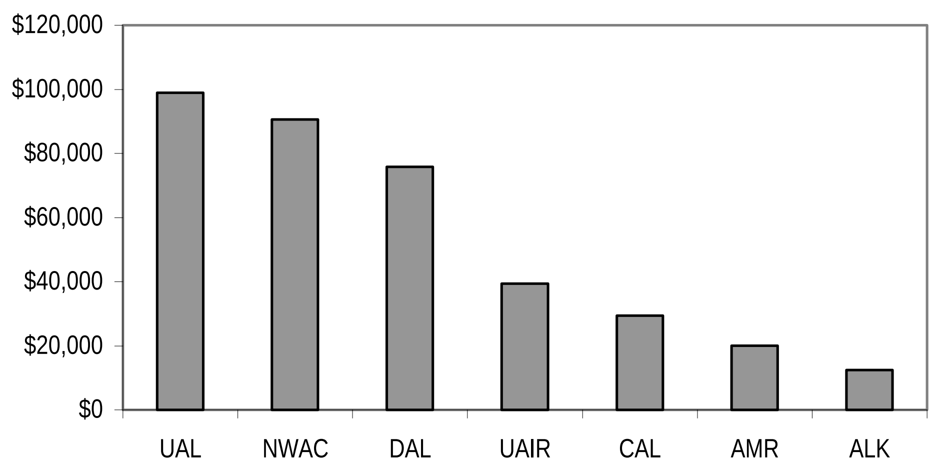
Exhibit 18. 2004 Pension, Profit-Sharing, and Retiree CASM (as reported)



Note: UAL is as of 2003.

Source: Bear, Stearns & Co. Inc. estimates.

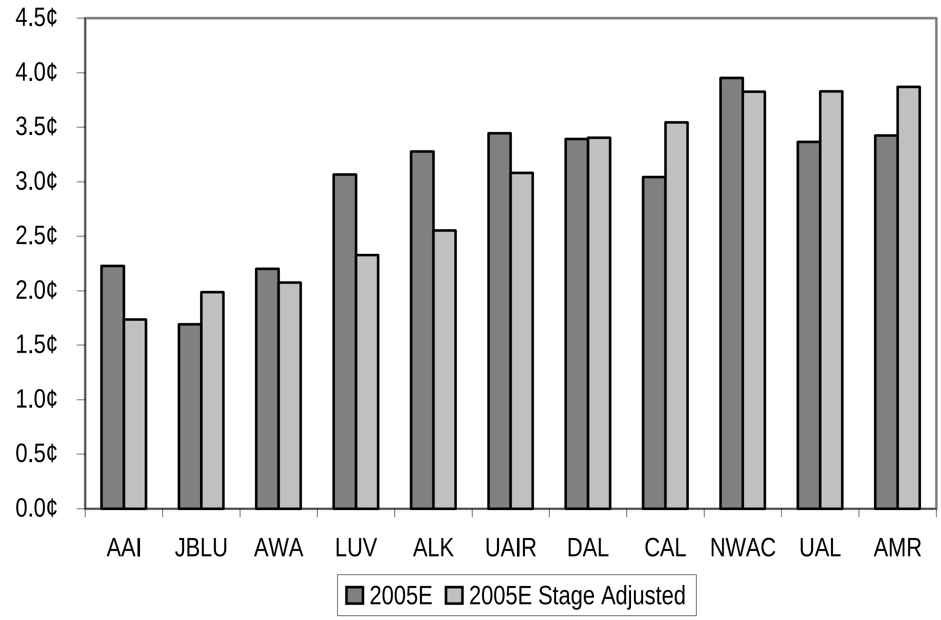
Exhibit 19. 2004 Unfunded ABO per Employee



Note: UAIR's defined benefit plans were terminated effective February 1, 2005 and UAL is attempting to do the same. UAL is calculated using 2003 ABOs and 2004 FTEs.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Exhibit 20. 2005E Labor CASM



Note: Stage-adjusted to 1,000 miles. UAIR and UAL are Not Rated. Using third-quarter 2004 stage as per Form 41 data

Source: Bear, Stearns & Co. Inc. estimates.

In 2005, given expiring pension legislation (plan years beginning after December 28, 2005 would revert to prior pension law), we expect Congress to attempt to replace current discount rate guidelines. In addition, airline labor leaders have recently espoused a mechanism whereby airlines could spread out their deficit reduction contributions over many years. Further, with UAL working to terminate its DB pension plans and US Airways having successfully ditched its own, those carriers not operating under the auspices of Chapter 11 (22), could find themselves at a substantial disadvantage, particularly given the significant hurdles required for terminating a plan outside of bankruptcy: 1) meeting PBGC's "financial distress" test, and 2) obtaining labor union consent to the changes.

Exhibit 21. Pension Cash Contribution Estimates ($ in millions)

	Required Pension Cash Contributions				
	ALK	AMR	CAL	DAL	NWAC
2004	$49	$467	$0	$455	$253
2005E	$58	$310	$192	$275	$420
2005E Pension Cash as % of Op. Cash Flow	19%	28%	63%	61%	126%
2006E Plan Freezes and 20-Yr Amort.	$4	$45	$44	$202	$133
2006E Bush Proposal (7-Yr Amort.)	$71	$314	$288	$726	$704
2006E PFEA Expires and 5-Yr Amort.	$76	$377	$356	$962	$901
2006E Plan Freezes and 20-Yr Amort. as % of Op. Cash Flow	1%	2%	6%	13%	11%
2006E Bush Proposal (7-Yr Amort.) as % of Op. Cash Flow	21%	16%	36%	47%	58%
2006E PFEA Expires and 5-Yr Amort. as % of Op. Cash Flow	23%	19%	45%	62%	74%

Note: 2004 and 2005 from company guidance and Bear Stearns estimates. 2006 hypothetical figures from Bear Stearns. Calculation methodology: Uses 2004 ABO funding level for ALK, AMR, CAL, DAL, and NWAC; 2006 DRC amortization is arrived at by assuming funding needed to achieve 90% ABO funding level (analogous to ERISA's current liability measure): 1) begin 2006 with 2005 estimated contribution amount, and haircut by 50% to arrive at non-DRC assumed contribution for 2006; 2) add estimated DRC amortizations deferred from 2004 and 2005 (2003 as well if any); and 3) add 2006 DRC amortization estimate. NWAC includes amortization from 2003 waived amount of $454 million. CAL has reached tentative labor agreements, which, if ratified, could freeze its DB plans and significantly lower pension funding requirements.

Source: Bear, Stearns & Co. Inc. estimates.

ALASKA AIR GROUP

Exhibit 22. Alaska Air's Pension Summary
($ in millions, except CASM data)

2004 PBO Funding Status	67%
2004 PBO Underfunding	($303)
2004 Defined Benefit Pension Expense	$78
2004 Defined Contribution + Profit-Sharing Expense	$25
2004 Retirement Health Care Expense (OPEB)	$9
2004 DB, DC, OPEB CASM	0.44¢
2005E DB Pension Cash Contributions	$58
2005E Operating Cash Flow (oil avg. $46/bbl)	$302
2004 Unrestricted Cash Balance	$874
2006E DB Pension Cash Contributions Base Case	$71
2006E Operating Cash Flow (oil avg $40/bbl)	$332

Source: Bear, Stearns & Co. Inc. estimates; company reports.

We believe Alaska Air Group has the least pension risk among our legacy carrier coverage universe. Our estimates suggest that Alaska Air's pension is underfunded by $300 million, or 33% on a PBO basis (21% on an ABO basis), better than the 41% average among the legacies; also, the $58 million in required cash contributions as a percentage of operating cash flow is 19%, well below the 50% group aggregate. Further, our estimated required contributions over the next two years are just 15% of the carrier's fourth-quarter 2004 unrestricted cash balance, versus the 34% group average.

For example, 2005 cash contributions are only expected to rise 18%, to $58 million, versus 66% at Northwest. In addition, the smaller carrier has lower absolute pension liabilities (liabilities are one-tenth the size of AMR's) and cash pension contributions are likely to be less meaningful for Alaska Air than the rest of the bunch. For instance, Alaska Air's 2005 cash contributions amount to just 7% of its fourth-quarter 2004 unrestricted cash balance, roughly one half of the other carriers' 13% average. Looked at as a percentage of 2005 estimated operating cash flow, Alaska Air's cash funding needs are half those of its nearest competitor.

Our sense is that given Alaska Air's relatively superior funding levels, stronger balance sheet (71% net debt to total invested capital versus the 114% average at the four nonbankrupt legacy airlines), and less burdensome near-term cash funding needs, the carrier is less likely to freeze its plans despite being in contract negotiations with the majority of its labor groups. While we estimate that Alaska Air enjoys a 28% labor CASM advantage to the network carriers, plan terminations at other carriers would reduce its current advantage to 19% for 2005 on a stage-adjusted basis.

Exhibit 23. AMR's Pension Summary
($ in millions, except CASM data)

2004 PBO Funding Status	73%
2004 PBO Underfunding	($2,687)
2004 Defined Benefit Pension Expense	$427
2004 Defined Contribution + Profit-Sharing Expense	$163
2004 Retirement Health Care Expense (OPEB)	$264
2004 DB, DC, OPEB CASM	0.46¢
2005E DB Pension Cash Contributions	$310
2005E Operating Cash Flow (oil avg. $46/bbl)	$1,089
2004 Unrestricted Cash Balance	$2,929
2006E DB Pension Cash Contributions Base Case	$314
2006E Operating Cash Flow (oil avg $40/bbl)	$1,982

Source: Bear, Stearns & Co. Inc. estimates; company reports.

We rank AMR's pension risk behind Alaska's, but ahead of Northwest's, Delta's, and Continental's. We estimate that AMR's pension is underfunded by $2.7 billion, or 27% on an PBO basis (20% on an ABO basis), better than the 41% average among the legacies; also, the $310 million in required cash contributions as a percentage of operating cash flow is 28%, below the 50% group aggregate. Further, our estimated required contributions over the next two years are 21% of the carrier's fourth-quarter 2004 unrestricted cash balance, versus the 34% group average.

AMR will likely contribute $310 million (absent legislative relief in 2005, the sum would have been much greater) in cash to its pensions in 2005, 11% of the company's unrestricted cash level, according to its December 31 balance sheet. This sizable cash outlay equates to roughly 28% (better than the group aggregate of 50%) of our 2005 operating cash flow estimate, equivalent to $1.24 in cash per share.

With its credit facility recently renegotiated, AMR should be able to easily meet 2005's cash obligations. In fact, AMR made a first installment in January 2005 of $42 million. However, looking to 2006, assuming no new pension legislation, we forecast cash contributions will rise 22%, to $377 million, or 19% of our operating cash flow estimate (our 2006 cash flow estimate assumes $40/bbl oil). To relieve this burden, AMR could seek IRS waivers should Congress fail to produce additional laws that benefit airlines with DB plans.

In addition, we expect AMR to seriously consider selling its investment arm, which it attempted to do in 2003, but pulled it off the market when bids failed to meet expectations. As a reference to that unit's potential value, we looked at M&A activity in the asset management industry over the past couple of years and concluded that its current assets under management imply a value of $400-$750 million for the money manager depending on the amount of assets ultimately transferred and relative performance (assumes price to assets under management of 2%-3% and total assets sold of $20-$25 billion).

Exhibit 24. Hypothetical Values for Asset Management Firms

	Assets Under Management (AUM) (US$ in billions)			
	$15	$20	$25	$30
Price to AUM Ratio	Implied Value of Asset Management Unit (US$ in millions)			
1.5%	$225	$300	$375	$450
2.0%	$300	$400	$500	$600
2.5%	$375	$500	$625	$750
3.0%	$450	$600	$750	$900
3.5%	$525	$700	$875	$1,050
4.0%	$600	$800	$1,000	$1,200

American Beacon Advisors directly managed or served as fiduciary or financial advisor for $37.6 billion in assets at 1/31/05, consisting of $17.3 billion under active management and $20.3 billion as named fiduciary or financial adviser.

Source: Bear, Stearns & Co. Inc. estimates.

In addition, AMR might be tempted to spin off part of its regional subsidiaries, just as Continental and Northwest did in 2002 and 2003. Given the right market conditions, that could conceivably raise $500 million to $1 billion, depending on the carrier's profit margin. (See the table below for potential margins and multiples.)

Exhibit 25. Regional Units Could Potentially Help Fund Pension Plans

Parent (former)	CAL XJT	NWAC PNCL	AMR Eagle + Exec.	SKYW	DAL ASA + Comair	Mean
ASMs (billions)	4.77	2.22	4.54	1.70	8.59	
Revenue (millions)	$1,461	$581	$1,820	$1,067	$2,117	
EBT Margin Actual (Assumed)	13%	11%	6%	12%	6%	12%
P/E Actual (Assumed)	6.6x	4.2x	7.1x	10.4x	7.1x	7.1x
Actual (Implied) Market Cap.	$604	$223	$496	$1,012	$577	
Assuming 12% EBT Margin			$988		$1,149	
10% of 2003 DB Plan Assets = Potential Contribution Ceiling			$734		$684	

Note: Second-half 2004 Scheduled ASMs from OAG via BACK Aviation; Revenue = 12 months ended 9/30/04. Comair and ASA revenues 12 months ended 6/30/04 using OD1A data. Market capitalization for XJT, PNCL, and SKYW as of 3/10/05. As reference, NWAC contributed $350 million (roughly 7% of total GAAP plan assets at 12/03) worth of privately held Pinnacle shares to its defined benefit plans in 2003. CAL contributed $100 million of XJT to its DB plans (approximately 8% of GAAP plan assets at 12/03), which was freely tradable. DAL paid over $2 billion for Comair and ASA according to media reports. Assumes 36% tax rate for wholly owned subsidiary implied market value calculations.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Exhibit 26. Continental's Pension Summary
($ in millions, except CASM data)

2004 PBO Funding Status	45%
2004 PBO Underfunding	($1,582)
2004 Defined Benefit Pension Expense	$293
2004 Defined Contribution + Profit-Sharing Expense	$30
2004 Retirement Health Care Expense (OPEB)	NA
2004 DB, DC, OPEB CASM	0.38¢
2005E Required DB Pension Contributions	$307
2005E DB Pension Cash Contributions	$192
2005E Operating Cash Flow (oil avg. $46/bbl)	$307
2004 Unrestricted Cash Balance	$1,460
2006E DB Pension Cash Contributions Base Case	$288
2006E Operating Cash Flow (oil avg $40/bbl)	$798

Note: 2005 pension contributions exclude $65 million in stock and assume $50 million in savings from labor deals.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

We believe Continental's pension risk is higher than Alaska Air's and AMR's, but lower than both Northwest's and Delta's. We estimate that Continental's pension is underfunded by $1.6 billion, or 55% on a PBO basis (47% on an ABO basis), worse than the 41% average among the legacies; also, the $192 million in required cash contributions as a percentage of operating cash flow is 63%, a touch above the group aggregate of 50%. Further, our estimated required contributions over the next two years are 33% of the carrier's fourth-quarter 2004 unrestricted cash balance, in line with the group average.

Continental started out 2004 with the best-funded pension plan of the legacy carriers, on a current liability basis (cash purposes). Originally, Continental intended to contribute $300 million to maintain a 90% current liability status (a level that precludes DRC requirements). (Current liabilities are measured using ERISA/IRC formulas analogous to the GAAP ABO [Accumulated Benefit Obligation], which differs from the PBO [Projected Benefit Obligation], since it makes no assumption about future compensation levels, making it generally lower than the PBO.) However, bruising fuel prices and weak yields made liquidity preservation a top priority, and, in turn, Continental availed itself of the Pension Funding Equity Act (PFEA) of 2004, thereby eliminating its cash contribution in 2004.

The year 2005 looks more troublesome, though the carrier did use $65 million of ExpressJet equity as an initial contribution in January. Assuming Continental achieves its stated $50 million in pension contribution savings resulting from tentative labor agreements, we estimate cash contributions of $192 million, or $1.86 per share, representing 63% of our operating cash flow estimate, higher than 50% group aggregate. Nevertheless, as a percentage of its December 2004 unrestricted cash balance, 2005's pension requirements amount to a more manageable 13%, in line with the group's average. After January's ExpressJet contribution, based on ownership levels as of February 7, we estimate that Continental could potentially contribute another $65 million in ExpressJet shares (at which point we estimate plan assets would hit ERISA's 10% ownership cap permissible for pension plans) to its DB plans, further reducing cash outflow to roughly $127 million. (Continental has publicly stated its intention to unwind its ownership of XJT shares.)

DELTA AIR LINES

Exhibit 27. Delta's Pension Summary
($ in millions, except CASM data)

2004 PBO Funding Status	56%
2004 PBO Underfunding	($5,298)
2004 Defined Benefit Pension Expense	$549
2004 Defined Contribution + Profit-Sharing Expense	$150
2004 Retirement Health Care Expense (OPEB)	$76
2004 DB, DC, OPEB CASM	0.53¢
2005E DB Pension Cash Contributions	$275
2005E Operating Cash Flow (oil avg. $46/bbl)	$454
2004 Unrestricted Cash Balance	$1,799
2006E DB Pension Cash Contributions Base Case	$726
2006E Operating Cash Flow (oil avg $40/bbl)	$1,558

Source: Bear, Stearns & Co. Inc. estimates; company reports.

We believe Delta has one the highest pension risk profiles among the legacy carriers operating outside of Chapter 11. While its funding deficit is the worst in the industry, its contributions as a percentage of cash flow are slightly below Northwest's. We estimate that Delta's pension is underfunded by $5.3 billion, or 44% on a PBO basis (43% on an ABO basis), greater than the 41% average among the legacies; also, the $275 million in required cash contributions as a percentage of operating cash flow is 61%, a notch above the 50% group aggregate. Further, our estimated required contributions over the next two years are a sizable 56% of the carrier's fourth-quarter 2004 unrestricted cash balance, versus the 34% group average.

On November 11, 2004, Delta's pilots ratified a new labor agreement principally calling for a 32.5% wage cut combined with a partial freezing of its defined benefit plan and subsequent creation of a defined contribution replacement plan. While the contract permitted Delta to avoid a potential fourth-quarter 2004 bankruptcy filing, the carrier has only scratched the surface regarding its pension underfunding. Despite freezing its pilot DB plan, Delta will still need to contribute hundreds of millions of dollars per year as a result of the $4 billion plus funding gap. What's more, the latest collective bargaining agreement established a new defined contribution requiring company funds, which will likely offset some of the potential cash savings.

For 2005, we estimate defined benefit pension cash contributions of $275 million (nonqualified DB plans will add another $65 million, while defined contribution plans could total $110 million), which is roughly 60% of our projected operating cash flow in that year. Further, as a percentage of its fourth-quarter 2004 cash balance, Delta's 2005 pension needs sit at roughly 15%, in line with the group average.

In light of the still-substantial pension obligations, Delta continues to face a formidable challenge — meeting its legally mandated funding requirements. The company posted the largest absolute funding gap of the nonbankrupt carriers in 2004, with an ABO underfunding of $5.2 billion versus runner-up Northwest's $3.6 billion in already-accrued unfunded liabilities. That said, we expect the company to pursue any and all non-termination outlets available to mitigate its pension burden. For example, in mid-December 2004, CEO Gerald Grinstein indicated Delta would work with Congress to devise a mechanism that would stretch out pension funding payments. Similarly, CFO Michael Palumbo has drawn analogies to funding deferrals obtained at both TWA and PanAm. In addition, we would not be surprised if Delta looked to spin off part of its regional subsidiaries, Comair and ASA, which it paid $2 billion-plus for in the 1980s and 1990s. (For more on this topic, see the exhibit below.)

Exhibit 28. Regional Units Could Potentially Help Fund Pension Plans

Parent (former)	CAL	NWAC	AMR		DAL	
	XJT	PNCL	Eagle + Exec.	SKYW	ASA + Comair	Mean
ASMs (billions)	4.77	2.22	4.54	1.70	8.59	
Revenue (millions)	$1,461	$581	$1,820	$1,067	$2,117	
EBT Margin Actual (Assumed)	13%	11%	6%	12%	6%	12%
P/E Actual (Assumed)	6.6x	4.2x	7.1x	10.4x	7.1x	7.1x
Actual (Implied) Market Cap.	$604	$223	$496	$1,012	$577	
Assuming 12% EBT Margin			$988		$1,149	
10% of 2003 DB Plan Assets = Potential Contribution Ceiling			$734		$684	

Note: Second-half 2004 Scheduled ASMs from OAG via BACK Aviation; Revenue = 12 months ended 9/30/04. Comair and ASA revenues 12 months ended 6/30/04 using OD1A data. Market capitalization for XJT, PNCL, and SKYW as of 3/10/05. As reference, NWAC contributed $350 million (roughly 7% of total GAAP plan assets at 12/03) worth of privately held Pinnacle shares to its defined benefit plans in 2003. CAL contributed $100 million of XJT to its DB plans (approximately 8% of GAAP plan assets at 12/03), which was freely tradable. DAL paid over $2 billion for Comair and ASA according to media reports. Assumes 36% tax rate for wholly owned subsidiary implied market value calculations.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

NORTHWEST AIRLINES

Exhibit 29. Northwest's Pension Summary
($ in millions, except CASM data)

2004 PBO Funding Status	59%
2004 PBO Underfunding	($3,820)
2004 Defined Benefit Pension Expense	$444
2004 Defined Contribution + Profit-Sharing Expense	NA
2004 Retirement Health Care Expense (OPEB)	$98
2004 DB, DC, OPEB CASM	0.59¢
2005E DB Pension Cash Contributions	$420
2005E Operating Cash Flow (oil avg. $46/bbl)	$333
2004 Unrestricted Cash Balance	$2,459
2006E DB Pension Cash Contributions Base Case	$704
2006E Operating Cash Flow (oil avg $40/bbl)	$1,214

Source: Bear, Stearns & Co. Inc. estimates; company reports.

Northwest's cash contributions as a percentage of operating cash flow rank the highest among the legacy carriers. We estimate that Northwest's pension is underfunded by $3.8 billion, or 41% on a PBO basis (40% on an ABO basis), in line with the legacy average; also, the $420 million in required cash contributions as a percentage of operating cash flow is a whopping 126%, well above the 50% group aggregate. Further, our estimated required contributions over the next two years total

46% of the carrier's fourth-quarter 2004 unrestricted cash balance, versus the 34% group average.

In 2002-03, Northwest demonstrated to the markets its ability to tackle near-term pension requirements through cash, pension waivers, and noncash contributions. However, in doing so, the Minneapolis-based carrier expended several precious resources that may be difficult, if not impossible, to replicate this time around. In 2003, Northwest sought administrative relief and received permission to fund its pension plans with $223 million (for the 2002 plan year) in a subsidiary's stock and amortize 2003's payment of $454 million over five years. The Pension Funding Equity Act of 2004 reduced Northwest's 2004 cash contribution to $253 million. For 2005, the carrier expects pension needs to rise to $420 million, which amounts to 126% of our forecasted operating cash flow for the same year (more than double the group aggregate). However, as a percentage of fourth-quarter 2004's unrestricted cash balance, Northwest's pension cash requirements come in at 17%, only a touch north of the group average.

After successfully monetizing its regional subsidiary in 2003, Northwest is left with only an 11% stake, valued at roughly $25 million, hardly enough to make a meaningful dent in pension cash needs. Meeting 2005's pension needs should not present any extreme difficulties for the carrier, though turning to 2006, things may get uncomfortable should Congress allow the current legislation to expire without any replacement. The pilots union appears to understand the severity of the situation, as it recently agreed to discuss a possible DB freeze with the company in order to ensure the plan's sustainability. The pilots' freeze initiative could establish an important precedent for other unions that are in negotiations.

Aside from union concessions, the carrier still possesses two pension waivers (three remain for the pilots' plan) that it could apply for beginning in 2006 should Congress not act.

Notwithstanding the availability of additional pension waivers, we believe it could be more difficult to convince the IRS of the carrier's temporary financial hardship this time around (are the industry's current woes truly temporary?) as well as meet any additional collateral requirements that could be required. We note that in the first waiver application, Northwest was obligated to grant its pension plans liens on some domestic slots, international routes, aircraft, and engines, likely leaving less unencumbered assets for another round of waivers.

On a related front, Northwest received an informal request from the SEC regarding its pension plan accounting (GAAP) assumptions. Our initial take is that while it is a noncash issue, Northwest's asset allocation (74%-20% equities/fixed income versus 63%-29% average at other carriers) is likely behind the higher return expectation. Should Northwest move to reduce its expected rate of return assumption by 50 bps, all else equal, we estimate that it could negatively affect expenses by roughly $27 million, or $0.20 per share.

UNITED AIRLINES AND US AIRWAYS (BOTH NOT RATED)

US Airways terminated its remaining defined benefit plans in January 2005 (in its first stint in bankruptcy, US Airways terminated its pilots' defined benefit pension plan). The much larger United appears to be in a more tenuous situation, as the PBGC preemptively moved in late December 2004 to terminate the pilots' plan, in hopes that relief from cockpit crew DB plans would allow the airline to maintain the remainder of its plans, something UAL vigorously opposes. United's pilots union agreed in its latest contract (ratified in January) not to fight its DB plan's termination, in return for a healthy DC plan and a $550 million convertible note to supplement the pension benefit losses. The large convertible note could pose a sticking point for other unions and potential exit financiers. However, punting the pilots' plan alone could save $1.3 billion (30% of total pension cash obligations due through 2008) in cash contributions. Subsequently, the PBGC also moved in mid-March to take over the UAL ground workers pension plan, which is estimated to require the greatest funding contributions of all of UAL's plans through 2008, at $1.4 billion. Relieved of the responsibility for its two costliest plans, UAL could find it tougher to convince a judge of the need to terminate the remaining plans.

UAL faces substantial pension contributions in the coming years. It continues to hemorrhage cash, similar to the other legacy airlines, and the difficulty in attracting exit financing has all but sealed the fate of its defined benefit plans, in our view. Through 2009, UAL estimated it would have to contribute more than $4 billion. Should UAL also succeed in terminating all of its defined benefit plans, while also reducing wage rates, and exit with low-cost carrier-like costs, the second-largest U.S. airline would pose a formidable challenge for fellow legacy and LCC carriers alike, in our opinion. In addition, any changes made to UAL's pension plans are likely to ripple through the industry given the carrier's size, spurring modifications at other airlines.

Exhibit 30. There Appears to Be No Way Around Huge Cash Drain Except Termination

UAL Minimum DB Funding Contributions (US$ in millions)(1)	No Waiver	Waiver
2005E	$1,200	$200
2006E	$1,000	$400
2007E	$1,500	$1,000
2008E	$600	$1,400
2009E	$100	$1,200
2010E	$0	$500
Total	$4,400	$4,800

US Airways Minimum DB Funding Contributions (US$ in millions)(2)	No Waiver	Freeze & Waiver
2005E		$32
2006E		$59
2007E		$177
2008E		$213
2009E		$248
Total	$987	$728

(1) Company reports dated 12/15/04; due to rounding, breakdown as shown in millions does not foot with company-disclosed total of $4.8 billion.
(2) Court fillings 12/13/04; assumes IAM/AFA plan freezes 1/1/05 and waivers from 2004-06 as well as waivers for the CE plan from 2007-09.

Source: Bear, Stearns & Co. Inc. estimates; company reports.

A QUICK OVERVIEW

As plan assets fall at the airlines, pension obligations become an issue, particularly for those carriers with "defined benefit" plans, which differ from 401k plans because the DB sponsor bears all the investment risk by guaranteeing a retirement amount. Carriers with defined benefit plans include Alaska Air Group, American Airlines, Continental, Delta, Northwest, United, and US Airways. Southwest, JetBlue, AirTran, Frontier, and America West do not offer defined benefit plans, though they do provide defined contribution plans partially funded by the carriers themselves.

On top of regular maintenance contributions, federal pension law requires companies to contribute additional assets unless the pension plan's funded status is at least 90% or the funded liability is currently at least 80% and was at least 90% in two consecutive years out of the past three. However, DRC funding rules are such that companies often have limited amounts of time to make up the shortfall and, under some circumstances, may contribute limited amounts of stock rather than cash. (In 2003, and again in January 2005, Northwest and Continental used stock to fund portions of their pension plans, and we expect AMR, Continental, and Delta to consider future cash funding alternatives.)

Over on the P&L, pension accounting permits the use of smoothing mechanisms that spread out recognition of income and expenses. Accordingly, it reduces the volatility of pension earnings (costs). What's more, the income or expense items in a given year are largely determined by the previous year's assumptions and plan realizations. For the most part, this suggests that companies have substantial visibility with regard to their current-year pension expense (and contributions) and to a lesser extent for the following year. Of course, the variability of key inputs, such as the discount rate, in pension forecasting makes longer-term estimates much less reliable. In addition, the legislative uncertainty only adds to the uncertainty of contribution forecasts beyond this year.

In terms of the balance sheet, if a plan's Accumulated Benefit Obligation (ABO) exceeds plan assets, then, at a minimum, the company must record the unfunded amount on its balance sheet.

Another important factor in pension calculations is the mortality rates mandated by federal law. Pension plans currently use the 1983 Group Annuity Mortality Table, which some argue fails to accurately reflect current longevity norms. The Secretary of the Treasury is empowered to update mortality figures based on projected trends and DB plans' actuarial experience. As a result, the Department of Treasury and the IRS are reviewing the mortality tables, which could lead to longer benefit stream assumptions.

In summary, defined benefit plans affect earnings through net pension costs (found in labor expenses at airlines), cash flows due to required cash contributions, and balance sheet equity due to any minimum pension liability charges (excess of accumulated benefit obligations over the fair value of plan assets). Conversely, pension accounting can provide a boost to earnings, as occurred in the late 1990s, when assets outperformed return expectations.

ERISA: BACKGROUND

There are three federal entities that administer and enforce ERISA for corporate pension plans: the Department of Labor (DOL), the Internal Revenue Service (IRS), and the Pension Benefit Guaranty Corporation (PBGC). The DOL's Employee Benefits Security Administration has the authority to allow exemptions to certain ERISA rules, such as contributions of in-kind securities to a DB plan. For its part, the IRS has the authority to grant waivers deferring current contribution requirements to the following year. The PBGC was created by ERISA to insure continuity of defined benefit plans and the orderly payment of benefits. Often this entails the PBGC taking over a failed DB plan. For example, as part of US Airways' two bankruptcies, the PBGC agreed to assume responsibility for all of its DB plans and ensure that retirees receive benefits. For this insurance, plan sponsors pay premiums to the PBGC, which increase with the size of their funding gap.

We note that pension payments are required on a quarterly basis. Each quarterly payment must be 25% of the annual amount, and it is due within 8.5 months of the plan's year-end. These payments are due on the fifteenth day of the fourth, seventh, tenth, and thirteenth month from the beginning of the plan year. Thus, a December year-end company would make its quarterly payments on April 15, July 15, October 15, and January 15, one month after the plan's year-end.

Appendix: Cash Burn and Oil Sensitivity

Exhibit 31. Cash Burn with No Debt Refinancing

With NO Debt Refinancing
As of 3/11/05

Cash Flow/Burn 2005E (US$ millions)	AMR[2]	CAL	DAL[3]	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[4]
2005E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,004	$686	$1,191	$889	$182	$897	$61	$375	$114	$16
Operating CF (after-tax) $35/bbl	$1,699	$560	$945	$704	$166	$886	$46	$351	$72	$9
Operating CF (after-tax) $40/bbl	$1,394	$433	$699	$518	$151	$875	$32	$327	$30	$1
Operating CF (after-tax) $45/bbl (Base Case)	$1,089	$307	$454	$333	$135	$864	$19	$302	($12)	($6)
Operating CF (after-tax) $50/bbl	$784	$181	$208	$147	$120	$853	$6	$278	($54)	($13)
Operating CF (after-tax) $55/bbl	$479	$55	($38)	($38)	$104	$842	($7)	$254	($96)	($21)
Cash Obligations										
Net Capex	$517	$170	$500	$200	$100	$380	$73	$170	$45	$35
DB Pension Contributions[5]	$310	$192	$275	$420	NA	NA	NA	$58	NA	NA
Cash From Financings	$0	$0	($250)	($107)	$0	($296)	$0	$0	($20)	$0
Debt Maturities	$910	$688	$630	$749	$105	$146	$14	$54	$102	$17
Liquidity										
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
Unrestricted Cash Balance at Calendar 3Q04	$3,135	$1,539	$1,446	$2,541	$517	$1,876	$339	$879	$417	$160
2005E Cash Flow (Burn) Oil @ $30/bbl	$267	($364)	$36	($373)	($24)	$668	($25)	$94	($12)	($36)
Cash Flow (Burn) per Day $30/bbl	$0.7	($1.0)	$0.1	($1.0)	($0.1)	$1.8	($0.1)	$0.3	($0.0)	($0.1)
2005E End of Year Unrestricted Cash $30/bbl	$3,196	$1,096	$1,835	$2,086	$425	$1,973	$309	$968	$294	$113
Months of Cash Left with Oil at $30/bbl from YE 2004 to Threshold	CF Pos.	12+	CF Pos.	12+	12+	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $35/bbl	($38)	($490)	($210)	($559)	($39)	$656	($40)	$70	($54)	($43)
Cash Flow (Burn) per Day $35/bbl	($0.1)	($1.3)	($0.6)	($1.5)	($0.1)	$1.8	($0.1)	$0.2	($0.1)	($0.1)
2005E End of Year Unrestricted Cash $35/bbl	$2,891	$970	$1,589	$1,900	$410	$1,961	$294	$943	$251	$106
Months of Cash Left with Oil at $35/bbl from YE 2004 to Threshold	12+	11	12+	12+	12+	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $40/bbl	($343)	($617)	($456)	($744)	($55)	$645	($54)	$45	($97)	($51)
Cash Flow (Burn) per Day $40/bbl	($0.9)	($1.7)	($1.2)	($2.0)	($0.1)	$1.8	($0.1)	$0.1	($0.3)	($0.1)
2005E End of Year Unrestricted Cash $40/bbl	$2,586	$843	$1,343	$1,715	$395	$1,950	$280	$919	$209	$98
Months of Cash Left with Oil at $40/bbl from YE 2004 to Threshold	12+	9	8	12+	12+	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $45/bbl (Base Case)	($648)	($743)	($701)	($930)	($70)	$634	($68)	$21	($139)	($58)
Cash Flow (Burn) per Day $45/bbl	($1.8)	($2.0)	($1.9)	($2.5)	($0.2)	$1.7	($0.2)	$0.1	($0.4)	($0.2)
2005E End of Year Unrestricted Cash $45/bbl	$2,281	$717	$1,098	$1,529	$379	$1,939	$266	$895	$167	$91
Months of Cash Left with Oil at $45/bbl from YE '04 to Threshold	12+	7	5	12+	12+	CF Pos.	12+	CF Pos.	9	12+
2005E Cash Flow (Burn) Oil @ $50/bbl	($953)	($869)	($947)	($1,115)	($86)	$623	($81)	($3)	($181)	($65)
Cash Flow (Burn) per Day $50/bbl	($2.6)	($2.4)	($2.6)	($3.1)	($0.2)	$1.7	($0.2)	($0.0)	($0.5)	($0.2)
2005E End of Year Unrestricted Cash $50/bbl	$1,976	$591	$852	$1,344	$364	$1,928	$254	$871	$125	$84
Months of Cash Left with Oil at $50/bbl from YE 2004 to Threshold	12+	6	4	12+	12+	CF Pos.	12+	12+	7	12+
2005E Cash Flow (Burn) Oil @ $55/bbl	($1,258)	($995)	($1,193)	($1,301)	($101)	$612	($93)	($27)	($223)	($73)
Cash Flow (Burn) per Day $55/bbl	($3.4)	($2.7)	($3.3)	($3.6)	($0.3)	$1.7	($0.3)	($0.1)	($0.6)	($0.2)
2005E End of Year Unrestricted Cash $55/bbl	$1,671	$465	$606	$1,158	$348	$1,917	$241	$847	$83	$76
Months of Cash Left with Oil at $55/bbl from YE 2004 to Threshold	12+	6	3	12+	12+	CF Pos.	12+	12+	6	12+

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. Incorporates hedge positions.
(2) Assumes AMR has to repurchase $104 million facilities bond due in 4Q05.
(3) Assumes drawdown on $250 million of available Amex prepayment.
(4) FRNT is in 2006 March-ending fiscal year, base assumption oil at $43.75/bbl for FY2006.
(5) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	$1,500	$1,000	$1,500	$1,100	$150	$750	$100	$300	$200	$75

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 32. Cash Burn Assuming 80% Debt Refinancing

With Debt Refinancing of 80% of Maturing Amount
As of 3/11/05

Cash Flow/Burn 2005E (US$ millions)	AMR[2]	CAL	DAL[3]	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[4]
2005E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,004	$686	$1,191	$889	$182	$897	$61	$375	$114	$16
Operating CF (after-tax) $35/bbl	$1,699	$560	$945	$704	$166	$886	$46	$351	$72	$9
Operating CF (after-tax) $40/bbl	$1,394	$433	$699	$518	$151	$875	$32	$327	$30	$1
Operating CF (after-tax) $45/bbl (Base Case)	$1,089	$307	$454	$333	$135	$864	$19	$302	($12)	($6)
Operating CF (after-tax) $50/bbl	$784	$181	$208	$147	$120	$853	$6	$278	($54)	($13)
Operating CF (after-tax) $55/bbl	$479	$55	($38)	($38)	$104	$842	($7)	$254	($96)	($21)
Cash Obligations										
Net Capex	$517	$170	$500	$200	$100	$380	$73	$170	$45	$35
DB Pension Contributions[5]	$310	$192	$275	$420	NA	NA	NA	$58	NA	NA
Cash From Financings	$0	$0	($250)	($107)	$0	($296)	$0	$0	($20)	$0
Debt Maturities	$182	$138	$126	$150	$21	$29	$3	$11	$20	$3
Liquidity										
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
Unrestricted Cash Balance at Calendar 3Q04	$3,135	$1,539	$1,446	$2,541	$517	$1,876	$339	$879	$417	$160
2005E Cash Flow (Burn) Oil @ $30/bbl	$995	$186	$540	$226	$61	$784	($14)	$136	$69	($22)
Cash Flow (Burn) per Day $30/bbl	$2.7	$0.5	$1.5	$0.6	$0.2	$2.1	($0.0)	$0.4	$0.2	($0.1)
2005E End of Year Unrestricted Cash $30/bbl	$3,924	$1,646	$2,339	$2,685	$510	$2,089	$320	$1,010	$375	$127
Months of Cash Left with Oil at $30/bbl from YE 2004 to Threshold	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	12+	CF Pos.	CF Pos.	12+
2005E Cash Flow (Burn) Oil @ $35/bbl	$690	$60	$294	$41	$45	$773	($29)	$112	$27	($30)
Cash Flow (Burn) per Day $35/bbl	$1.9	$0.2	$0.8	$0.1	$0.1	$2.1	($0.1)	$0.3	$0.1	($0.1)
2005E End of Year Unrestricted Cash $35/bbl	$3,619	$1,520	$2,093	$2,500	$494	$2,078	$305	$986	$333	$119
Months of Cash Left with Oil at $35/bbl from YE 2004 to Threshold	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	12+	CF Pos.	CF Pos.	12+
2005E Cash Flow (Burn) Oil @ $40/bbl	$385	($66)	$48	($145)	$30	$762	($43)	$88	($15)	($37)
Cash Flow (Burn) per Day $40/bbl	$1.1	($0.2)	$0.1	($0.4)	$0.1	$2.1	($0.1)	$0.2	($0.0)	($0.1)
2005E End of Year Unrestricted Cash $40/bbl	$3,314	$1,394	$1,847	$2,314	$479	$2,067	$291	$962	$290	$112
Months of Cash Left with Oil at $40/bbl from YE 2004 to Threshold	CF Pos.	12+	CF Pos.	12+	CF Pos.	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $45/bbl (Base Case)	$80	($192)	($197)	($330)	$14	$751	($57)	$64	($57)	($44)
Cash Flow (Burn) per Day $45/bbl	$0.2	($0.5)	($0.5)	($0.9)	$0.0	$2.1	($0.2)	$0.2	($0.2)	($0.1)
2005E End of Year Unrestricted Cash $45/bbl	$3,009	$1,268	$1,602	$2,129	$463	$2,056	$278	$938	$248	$105
Months of Cash Left with Oil at $45/bbl from YE '04 to Threshold	CF Pos.	12+	12+	12+	CF Pos.	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $50/bbl	($225)	($319)	($443)	($516)	($1)	$740	($69)	$40	($100)	($52)
Cash Flow (Burn) per Day $50/bbl	($0.6)	($0.9)	($1.2)	($1.4)	($0.0)	$2.0	($0.2)	$0.1	($0.3)	($0.1)
2005E End of Year Unrestricted Cash $50/bbl	$2,704	$1,141	$1,356	$1,943	$448	$2,045	$265	$914	$206	$97
Months of Cash Left with Oil at $50/bbl from YE 2004 to Threshold	12+	12+	8	12+	12+	CF Pos.	12+	CF Pos.	12+	12+
2005E Cash Flow (Burn) Oil @ $55/bbl	($530)	($445)	($689)	($702)	($17)	$729	($82)	$16	($142)	($59)
Cash Flow (Burn) per Day $55/bbl	($1.5)	($1.2)	($1.9)	($1.9)	($0.0)	$2.0	($0.2)	$0.0	($0.4)	($0.2)
2005E End of Year Unrestricted Cash $55/bbl	$2,399	$1,015	$1,110	$1,757	$432	$2,034	$252	$890	$164	$90
Months of Cash Left with Oil at $55/bbl from YE 2004 to Threshold	12+	12+	5	12+	12+	CF Pos.	12+	CF Pos.	9	12+

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. Incorporates hedge positions.
(2) Assumes AMR has to repurchase $104 million facilities bond due in 4Q05.
(3) Assumes drawdown on $250 million of available Amex prepayment.
(4) FRNT is in 2006 March-ending fiscal year, base assumption oil at $43.75/bbl for FY2006.
(5) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	$1,500	$1,000	$1,500	$1,100	$150	$750	$100	$300	$200	$75

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 33. Cash Burn with No Debt Refinancing and PFEA Expiration (Five-Year Amortization)

With NO Debt Refinancing & PFEA Expiration (5-Yr Amortization)
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$377	$356	$962	$901	NA	NA	NA	$76	NA	NA
Debt Maturities	$1,328	$533	$733	$994	$108	$604	$10	$57	$100	$18
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$2,281	$717	$1,098	$1,529	$379	$1,939	$266	$895	$167	$91
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	$871	($14)	$7	($592)	($47)	$43	$89	$137	($63)	($18)
Cash Flow (Burn) per Day $30/bbl	$2.4	($0.0)	$0.0	($1.6)	($0.1)	$0.1	$0.2	$0.4	($0.2)	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$3,152	$703	$1,105	$937	$332	$1,983	$355	$1,033	$104	$73
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	Ch. 11 Risk	CF Pos.	9	59	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	11
2006E Cash Flow (Burn) Oil @ $35/bbl	$483	($139)	($330)	($751)	($73)	$6	$65	$105	($99)	($29)
Cash Flow (Burn) per Day $35/bbl	$1.3	($0.4)	($0.9)	($2.1)	($0.2)	$0.0	$0.2	$0.3	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $35/bbl	$2,764	$578	$767	$779	$306	$1,945	$331	$1,000	$68	$62
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	Ch. 11 Risk	Ch. 11 Risk	7	38	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	7
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	$67	($260)	($667)	($909)	($99)	($31)	$40	$72	($135)	($41)
Cash Flow (Burn) per Day $40/bbl	$0.2	($0.7)	($1.8)	($2.5)	($0.3)	($0.1)	$0.1	$0.2	($0.4)	($0.1)
2006E End of Year Unrestricted Cash $40/bbl	$2,348	$457	$430	$620	$280	$1,908	$307	$967	$32	$50
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold[5]	CF Pos.	Ch. 11 Risk	Ch. 11 Risk	6	28	454	CF Pos.	CF Pos.	Ch. 11 Risk	5
2006E Cash Flow (Burn) Oil @ $45/bbl	($350)	($380)	($1,004)	($1,067)	($125)	($69)	$16	$39	($171)	($52)
Cash Flow (Burn) per Day $45/bbl	($1.0)	($1.0)	($2.8)	($2.9)	($0.3)	($0.2)	$0.0	$0.1	($0.5)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$1,932	$337	$93	$462	$254	$1,871	$283	$934	($4)	$39
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	27	Ch. 11 Risk	Ch. 11 Risk	5	22	207	CF Pos.	CF Pos.	Ch. 11 Risk	4
2006E Cash Flow (Burn) Oil @ $50/bbl	($766)	($547)	($1,342)	($1,226)	($151)	($106)	($8)	$6	($207)	($63)
Cash Flow (Burn) per Day $50/bbl	($2.1)	($1.5)	($3.7)	($3.4)	($0.4)	($0.3)	($0.0)	$0.0	($0.6)	($0.2)
2006E End of Year Unrestricted Cash $50/bbl	$1,515	$170	NM	$304	$228	$1,833	$258	$902	($40)	$28
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	12	Ch. 11 Risk	Ch. 11 Risk	4	18	134	253	CF Pos.	Ch. 11 Risk	3
2006E Cash Flow (Burn) Oil @ $55/bbl	($1,182)	($715)	($1,679)	($1,384)	($177)	($144)	($32)	($26)	($243)	($75)
Cash Flow (Burn) per Day $55/bbl	($3.2)	($2.0)	($4.6)	($3.8)	($0.5)	($0.4)	($0.1)	($0.1)	($0.7)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$1,099	$2	NM	$145	$202	$1,796	$234	$869	($76)	$16
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	8	Ch. 11 Risk	Ch. 11 Risk	4	16	99	62	272	Ch. 11 Risk	3

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	$1,500	$1,000	$1,500	$1,100	$150	$750	$100	$300	$200	$75

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 34. Cash Burn with No Debt Refinancing and Bush Pension Proposal (Seven-Year Amortization)

With NO Debt Refinancing & Bush Proposal (7-Yr Amortization)
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$314	$288	$726	$704	NA	NA	NA	$71	NA	NA
Debt Maturities	$1,328	$533	$733	$994	$108	$604	$10	$57	$100	$18
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$2,281	$717	$1,098	$1,529	$379	$1,939	$266	$895	$167	$91
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	$935	$54	$243	($395)	($47)	$43	$89	$143	($63)	($18)
Cash Flow (Burn) per Day $30/bbl	$2.6	$0.1	$0.7	($1.1)	($0.1)	$0.1	$0.2	$0.4	($0.2)	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$3,216	$771	$1,340	$1,135	$332	$1,983	$355	$1,038	$104	$73
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	13	59	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	11
2006E Cash Flow (Burn) Oil @ $35/bbl	$547	($72)	($95)	($553)	($73)	$6	$65	$110	($99)	($29)
Cash Flow (Burn) per Day $35/bbl	$1.5	($0.2)	($0.3)	($1.5)	($0.2)	$0.0	$0.2	$0.3	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $35/bbl	$2,828	$645	$1,003	$976	$306	$1,945	$331	$1,005	$68	$62
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	Ch. 11 Risk	Ch. 11 Risk	9	38	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	7
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	$130	($193)	($432)	($711)	($99)	($31)	$40	$77	($135)	($41)
Cash Flow (Burn) per Day $40/bbl	$0.4	($0.5)	($1.2)	($1.9)	($0.3)	($0.1)	$0.1	$0.2	($0.4)	($0.1)
2006E End of Year Unrestricted Cash $40/bbl	$2,411	$524	$666	$818	$280	$1,908	$307	$972	$32	$50
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold[5]	CF Pos.	Ch. 11 Risk	Ch. 11 Risk	7	28	454	CF Pos.	CF Pos.	Ch. 11 Risk	5
2006E Cash Flow (Burn) Oil @ $45/bbl	($286)	($313)	($769)	($870)	($125)	($69)	$16	$44	($171)	($52)
Cash Flow (Burn) per Day $45/bbl	($0.8)	($0.9)	($2.1)	($2.4)	($0.3)	($0.2)	$0.0	$0.1	($0.5)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$1,995	$405	$329	$660	$254	$1,871	$283	$940	($4)	$39
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	33	Ch. 11 Risk	Ch. 11 Risk	6	22	207	CF Pos.	CF Pos.	Ch. 11 Risk	4
2006E Cash Flow (Burn) Oil @ $50/bbl	($702)	($480)	($1,106)	($1,028)	($151)	($106)	($8)	$12	($207)	($63)
Cash Flow (Burn) per Day $50/bbl	($1.9)	($1.3)	($3.0)	($2.8)	($0.4)	($0.3)	($0.0)	$0.0	($0.6)	($0.2)
2006E End of Year Unrestricted Cash $50/bbl	$1,579	$237	NM	$501	$228	$1,833	$258	$907	($40)	$28
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	13	Ch. 11 Risk	Ch. 11 Risk	5	18	134	253	CF Pos.	Ch. 11 Risk	3
2006E Cash Flow (Burn) Oil @ $55/bbl	($1,119)	($648)	($1,443)	($1,187)	($177)	($144)	($32)	($21)	($243)	($75)
Cash Flow (Burn) per Day $55/bbl	($3.1)	($1.8)	($4.0)	($3.3)	($0.5)	($0.4)	($0.1)	($0.1)	($0.7)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$1,162	$70	NM	$343	$202	$1,796	$234	$874	($76)	$16
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	8	Ch. 11 Risk	Ch. 11 Risk	4	16	99	62	337	Ch. 11 Risk	3

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital. Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	$1,500	$1,000	$1,500	$1,100	$150	$750	$100	$300	$200	$75

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 35. Cash Burn with No Debt Refinancing and Pension Plan Freeze/20-Year Amortization Proposal

With NO Debt Refinancing & Pension Plan Freeze / 20-Yr Amortization Proposal
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$45	$44	$202	$133	NA	NA	NA	$4	NA	NA
Debt Maturities	$1,328	$533	$733	$994	$108	$604	$10	$57	$100	$18
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$2,281	$717	$1,098	$1,529	$379	$1,939	$266	$895	$167	$91
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	$1,203	$298	$768	$176	($47)	$43	$89	$209	($63)	($18)
Cash Flow (Burn) per Day $30/bbl	$3.3	$0.8	$2.1	$0.5	($0.1)	$0.1	$0.2	$0.6	($0.2)	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$3,484	$1,015	$1,865	$1,705	$332	$1,983	$355	$1,104	$104	$73
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	59	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	11
2006E Cash Flow (Burn) Oil @ $35/bbl	$815	$172	$430	$17	($73)	$6	$65	$176	($99)	($29)
Cash Flow (Burn) per Day $35/bbl	$2.2	$0.5	$1.2	$0.0	($0.2)	$0.0	$0.2	$0.5	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $35/bbl	$3,096	$889	$1,528	$1,547	$306	$1,945	$331	$1,071	$68	$62
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	38	CF Pos.	CF Pos.	CF Pos.	Ch. 11 Risk	7
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	$398	$51	$93	($141)	($99)	($31)	$40	$143	($135)	($41)
Cash Flow (Burn) per Day $40/bbl	$1.1	$0.1	$0.3	($0.4)	($0.3)	($0.1)	$0.1	$0.4	($0.4)	($0.1)
2006E End of Year Unrestricted Cash $40/bbl	$2,680	$768	$1,191	$1,388	$280	$1,908	$307	$1,039	$32	$50
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	37	28	454	CF Pos.	CF Pos.	Ch. 11 Risk	5
2006E Cash Flow (Burn) Oil @ $45/bbl	($18)	($69)	($244)	($299)	($125)	($69)	$16	$111	($171)	($52)
Cash Flow (Burn) per Day $45/bbl	($0.0)	($0.2)	($0.7)	($0.8)	($0.3)	($0.2)	$0.0	$0.3	($0.5)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$2,263	$648	$854	$1,230	$254	$1,871	$283	$1,006	($4)	$39
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	526	Ch. 11 Risk	Ch. 11 Risk	17	22	207	CF Pos.	CF Pos.	Ch. 11 Risk	4
2006E Cash Flow (Burn) Oil @ $50/bbl	($434)	($236)	($581)	($458)	($151)	($106)	($8)	$78	($207)	($63)
Cash Flow (Burn) per Day $50/bbl	($1.2)	($0.6)	($1.6)	($1.3)	($0.4)	($0.3)	($0.0)	$0.2	($0.6)	($0.2)
2006E End of Year Unrestricted Cash $50/bbl	$1,847	$481	$516	$1,072	$228	$1,833	$258	$973	($40)	$28
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	22	Ch. 11 Risk	Ch. 11 Risk	11	18	134	253	CF Pos.	Ch. 11 Risk	3
2006E Cash Flow (Burn) Oil @ $55/bbl	($850)	($404)	($918)	($616)	($177)	($144)	($32)	$45	($243)	($75)
Cash Flow (Burn) per Day $55/bbl	($2.3)	($1.1)	($2.5)	($1.7)	($0.5)	($0.4)	($0.1)	$0.1	($0.7)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$1,431	$313	$179	$913	$202	$1,796	$234	$940	($76)	$16
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	11	Ch. 11 Risk	Ch. 11 Risk	8	16	99	62	CF Pos.	Ch. 11 Risk	3

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	$1,500	$1,000	$1,500	$1,100	$150	$750	$100	$300	$200	$75

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 36. Cash Burn with Debt Refinancing of 80% of Maturing Amount and PFEA Expiration (Five-Year Amortization)

With Debt Refinancing of 80% of Maturing Amount & PFEA Expiration (5-Yr Amortization)
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$377	$356	$962	$901	NA	NA	NA	$76	NA	NA
Debt Maturities	$266	$107	$147	$199	$22	$121	$2	$11	$20	$4
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$3,009	$1,268	$1,602	$2,129	$463	$2,056	$278	$938	$248	$105
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	$1,934	$413	$594	$203	$40	$527	$97	$183	$17	($3)
Cash Flow (Burn) per Day $30/bbl	$5.3	$1.1	$1.6	$0.6	$0.1	$1.4	$0.3	$0.5	$0.0	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$4,943	$1,680	$2,195	$2,332	$503	$2,583	$374	$1,121	$265	$101
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	109
2006E Cash Flow (Burn) Oil @ $35/bbl	$1,545	$287	$256	$45	$13	$489	$72	$150	($19)	($15)
Cash Flow (Burn) per Day $35/bbl	$4.2	$0.8	$0.7	$0.1	$0.0	$1.3	$0.2	$0.4	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $35/bbl	$4,555	$1,555	$1,858	$2,173	$477	$2,545	$350	$1,088	$229	$90
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	30	24
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	$1,129	$166	($81)	($114)	($13)	$452	$48	$118	($55)	($26)
Cash Flow (Burn) per Day $40/bbl	$3.1	$0.5	($0.2)	($0.3)	($0.0)	$1.2	$0.1	$0.3	($0.2)	($0.1)
2006E End of Year Unrestricted Cash $40/bbl	$4,138	$1,433	$1,521	$2,015	$451	$2,508	$326	$1,056	$193	$79
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold[5]	CF Pos.	CF Pos.	15	109	298	CF Pos.	CF Pos.	CF Pos.	10	14
2006E Cash Flow (Burn) Oil @ $45/bbl	$713	$46	($418)	($272)	($39)	$414	$24	$85	($91)	($38)
Cash Flow (Burn) per Day $45/bbl	$2.0	$0.1	($1.1)	($0.7)	($0.1)	$1.1	$0.1	$0.2	($0.2)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$3,722	$1,314	$1,183	$1,856	$425	$2,471	$302	$1,023	$157	$67
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	3	45	97	CF Pos.	CF Pos.	CF Pos.	6	9
2006E Cash Flow (Burn) Oil @ $50/bbl	$297	($121)	($755)	($431)	($65)	$377	$0	$52	($127)	($49)
Cash Flow (Burn) per Day $50/bbl	$0.8	($0.3)	($2.1)	($1.2)	($0.2)	$1.0	$0.0	$0.1	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $50/bbl	$3,306	$1,146	$846	$1,698	$399	$2,433	$278	$990	$121	$56
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	CF Pos.	27	2	29	58	CF Pos.	CF Pos.	CF Pos.	5	7
2006E Cash Flow (Burn) Oil @ $55/bbl	($120)	($289)	($1,092)	($589)	($91)	$340	($24)	$19	($163)	($60)
Cash Flow (Burn) per Day $55/bbl	($0.3)	($0.8)	($3.0)	($1.6)	($0.2)	$0.9	($0.1)	$0.1	($0.4)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$2,889	$979	$509	$1,540	$372	$2,396	$253	$957	$85	$44
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	151	11	1	21	41	CF Pos.	88	CF Pos.	4	6

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	$1,500	$1,000	$1,500	$1,100	$150	$750	$100	$300	$200	$75

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 37. Cash Burn with Debt Refinancing of 80% of Maturing Amount and Bush Pension Proposal (Seven-Year Amortization)

With Debt Refinancing of 80% of Maturing Amount & Bush Proposal (7-Yr Amortization)
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$314	$288	$726	$704	NA	NA	NA	$71	NA	NA
Debt Maturities	$266	$107	$147	$199	$22	$121	$2	$11	$20	$4
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$3,009	$1,268	$1,602	$2,129	$463	$2,056	$278	$938	$248	$105
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	$1,997	$480	$829	$401	$40	$527	$97	$188	$17	($3)
Cash Flow (Burn) per Day $30/bbl	$5.5	$1.3	$2.3	$1.1	$0.1	$1.4	$0.3	$0.5	$0.0	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$5,006	$1,748	$2,431	$2,529	$503	$2,583	$374	$1,126	$265	$101
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	109
2006E Cash Flow (Burn) Oil @ $35/bbl	$1,609	$354	$492	$242	$13	$489	$72	$155	($19)	($15)
Cash Flow (Burn) per Day $35/bbl	$4.4	$1.0	$1.3	$0.7	$0.0	$1.3	$0.2	$0.4	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $35/bbl	$4,618	$1,622	$2,093	$2,371	$477	$2,545	$350	$1,093	$229	$90
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	30	24
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	$1,193	$233	$155	$84	($13)	$452	$48	$123	($55)	($26)
Cash Flow (Burn) per Day $40/bbl	$3.3	$0.6	$0.4	$0.2	($0.0)	$1.2	$0.1	$0.3	($0.2)	($0.1)
2006E End of Year Unrestricted Cash $40/bbl	$4,202	$1,501	$1,756	$2,212	$451	$2,508	$326	$1,061	$193	$79
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold	CF Pos.	CF Pos.	CF Pos.	CF Pos.	298	CF Pos.	CF Pos.	CF Pos.	10	14
2006E Cash Flow (Burn) Oil @ $45/bbl	$776	$114	($182)	($75)	($39)	$414	$24	$90	($91)	($38)
Cash Flow (Burn) per Day $45/bbl	$2.1	$0.3	($0.5)	($0.2)	($0.1)	$1.1	$0.1	$0.2	($0.2)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$3,785	$1,381	$1,419	$2,054	$425	$2,471	$302	$1,028	$157	$67
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	7	165	97	CF Pos.	CF Pos.	CF Pos.	6	9
2006E Cash Flow (Burn) Oil @ $50/bbl	$360	($54)	($520)	($233)	($65)	$377	$0	$57	($127)	($49)
Cash Flow (Burn) per Day $50/bbl	$1.0	($0.1)	($1.4)	($0.6)	($0.2)	$1.0	$0.0	$0.2	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $50/bbl	$3,369	$1,214	$1,082	$1,896	$399	$2,433	$278	$995	$121	$56
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	CF Pos.	60	2	53	58	CF Pos.	CF Pos.	CF Pos.	5	7
2006E Cash Flow (Burn) Oil @ $55/bbl	($56)	($221)	($857)	($391)	($91)	$340	($24)	$25	($163)	($60)
Cash Flow (Burn) per Day $55/bbl	($0.2)	($0.6)	($2.3)	($1.1)	($0.2)	$0.9	($0.1)	$0.1	($0.4)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$2,953	$1,046	$745	$1,737	$372	$2,396	$253	$963	$85	$44
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	322	15	1	32	41	CF Pos.	88	CF Pos.	4	6

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	$1,500	$1,000	$1,500	$1,100	$150	$750	$100	$300	$200	$75

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Exhibit 38. Cash Burn with Debt Refinancing of 80% of Maturing Amount and Pension Plan Freeze/20-Year Amortization Proposal

With Debt Refinancing of 80% of Maturing Amount & Pension Plan Freeze / 20-Yr Amortization Proposal
As of 3/11/05

Cash Flow/Burn 2006E (US$ millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT[2]
2006E Operating Cash Flow[1]										
Operating CF (after-tax) $30/bbl	$2,787	$1,045	$2,232	$1,531	$249	$1,073	$108	$398	$95	$35
Operating CF (after-tax) $35/bbl	$2,398	$919	$1,895	$1,373	$223	$1,035	$84	$365	$60	$24
Operating CF (after-tax) $40/bbl (Base Case)	$1,982	$798	$1,558	$1,214	$197	$998	$60	$332	$24	$12
Operating CF (after-tax) $45/bbl	$1,566	$679	$1,220	$1,056	$171	$961	$36	$300	($12)	$1
Operating CF (after-tax) $50/bbl	$1,149	$511	$883	$897	$145	$923	$11	$267	($48)	($10)
Operating CF (after-tax) $55/bbl	$733	$344	$546	$739	$119	$886	($13)	$234	($84)	($22)
Cash Obligations										
Net Capex	$210	$170	$530	$228	$188	$426	$10	$128	$59	$35
DB Pension Contributions[3]	$45	$44	$202	$133	NA	NA	NA	$4	NA	NA
Debt Maturities	$266	$107	$147	$199	$22	$121	$2	$11	$20	$4
Liquidity										
Estimated Unrestricted Cash Balance at Calendar 4Q05[4]	$3,009	$1,268	$1,602	$2,129	$463	$2,056	$278	$938	$248	$105
Unrestricted Cash Balance at Calendar 4Q04	$2,929	$1,460	$1,799	$2,459	$449	$1,305	$334	$874	$306	$149
2006E Cash Flow (Burn) Oil @ $30/bbl	$2,266	$724	$1,354	$971	$40	$527	$97	$255	$17	($3)
Cash Flow (Burn) per Day $30/bbl	$6.2	$2.0	$3.7	$2.7	$0.1	$1.4	$0.3	$0.7	$0.0	($0.0)
2006E End of Year Unrestricted Cash $30/bbl	$5,275	$1,992	$2,956	$3,100	$503	$2,583	$374	$1,193	$265	$101
Months of Cash Left with Oil at $30/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	109
2006E Cash Flow (Burn) Oil @ $35/bbl	$1,877	$598	$1,017	$813	$13	$489	$72	$222	($19)	($15)
Cash Flow (Burn) per Day $35/bbl	$5.1	$1.6	$2.8	$2.2	$0.0	$1.3	$0.2	$0.6	($0.1)	($0.0)
2006E End of Year Unrestricted Cash $35/bbl	$4,886	$1,866	$2,618	$2,941	$477	$2,545	$350	$1,160	$229	$90
Months of Cash Left with Oil at $35/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	CF Pos.	30	24
2006E Cash Flow (Burn) Oil @ $40/bbl (Base Case)	$1,461	$477	$680	$654	($13)	$452	$48	$189	($55)	($26)
Cash Flow (Burn) per Day $40/bbl	$4.0	$1.3	$1.9	$1.8	($0.0)	$1.2	$0.1	$0.5	($0.2)	($0.1)
2006E End of Year Unrestricted Cash $40/bbl	$4,470	$1,745	$2,281	$2,783	$451	$2,508	$326	$1,127	$193	$79
Months of Cash Left with Oil at $40/bbl from YE '05 to Threshold	CF Pos.	CF Pos.	CF Pos.	CF Pos.	298	CF Pos.	CF Pos.	CF Pos.	10	14
2006E Cash Flow (Burn) Oil @ $45/bbl	$1,045	$358	$342	$496	($39)	$414	$24	$156	($91)	($38)
Cash Flow (Burn) per Day $45/bbl	$2.9	$1.0	$0.9	$1.4	($0.1)	$1.1	$0.1	$0.4	($0.2)	($0.1)
2006E End of Year Unrestricted Cash $45/bbl	$4,054	$1,625	$1,944	$2,624	$425	$2,471	$302	$1,094	$157	$67
Months of Cash Left with Oil at $45/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	97	CF Pos.	CF Pos.	CF Pos.	6	9
2006E Cash Flow (Burn) Oil @ $50/bbl	$628	$190	$5	$337	($65)	$377	$0	$124	($127)	($49)
Cash Flow (Burn) per Day $50/bbl	$1.7	$0.5	$0.0	$0.9	($0.2)	$1.0	$0.0	$0.3	($0.3)	($0.1)
2006E End of Year Unrestricted Cash $50/bbl	$3,637	$1,458	$1,607	$2,466	$399	$2,433	$278	$1,062	$121	$56
Months of Cash Left with Oil at $50/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	CF Pos.	CF Pos.	58	CF Pos.	CF Pos.	CF Pos.	5	7
2006E Cash Flow (Burn) Oil @ $55/bbl	$212	$23	($332)	$179	($91)	$340	($24)	$91	($163)	($60)
Cash Flow (Burn) per Day $55/bbl	$0.6	$0.1	($0.9)	$0.5	($0.2)	$0.9	($0.1)	$0.2	($0.4)	($0.2)
2006E End of Year Unrestricted Cash $55/bbl	$3,221	$1,290	$1,270	$2,308	$372	$2,396	$253	$1,029	$85	$44
Months of Cash Left with Oil at $55/bbl from YE 2005 to Threshold[5]	CF Pos.	CF Pos.	4	CF Pos.	41	CF Pos.	88	CF Pos.	4	6

(1) Operating Cash Flow = Net Income + D&A + pension expense; assumes no impact from change in net working capital.
Assumes crude price of $40/bbl in 2006. Incorporates hedge positions.
(2) FRNT is in 2007 March-ending fiscal year, base assumption oil at $40/bbl for calendar 2006.
(3) Assumes no additional noncash (stock of subsidiary) contribution to DB pension plans.
(4) Assumes crude price of $49/bbl in 1Q05 and $45/bbl in 2Q-4Q05. For no debt refinancing scenario in 2006, assumes no debt refinancing in 2005. For debt refinancing scenario in 2006, assumes debt refinancing in 2005.
(5) Chapter 11 risk: operating with cash burn and cash balance is below threshold cash level.

(US$ in millions)	AMR	CAL	DAL	NWAC	JBLU	LUV	AAI	ALK	AWA	FRNT
Estimated Unrestricted Cash Concern Level	$1,500	$1,000	$1,500	$1,100	$150	$750	$100	$300	$200	$75

As points of reference, we note that AMR achieved its last-minute deal with labor last April with $1.2 billion (7% of LTM sales) in unrestricted cash and equivalents, UAL filed for Chapter 11 on 12/9/02 with $1.3 billion (9% of LTM sales) in unrestricted cash and equivalents (YE 2002), and US Air entered Chapter 11 on 8/11/02 with close to $900 million in cash (3Q02 balance was $900 million) (13% of LTM sales).

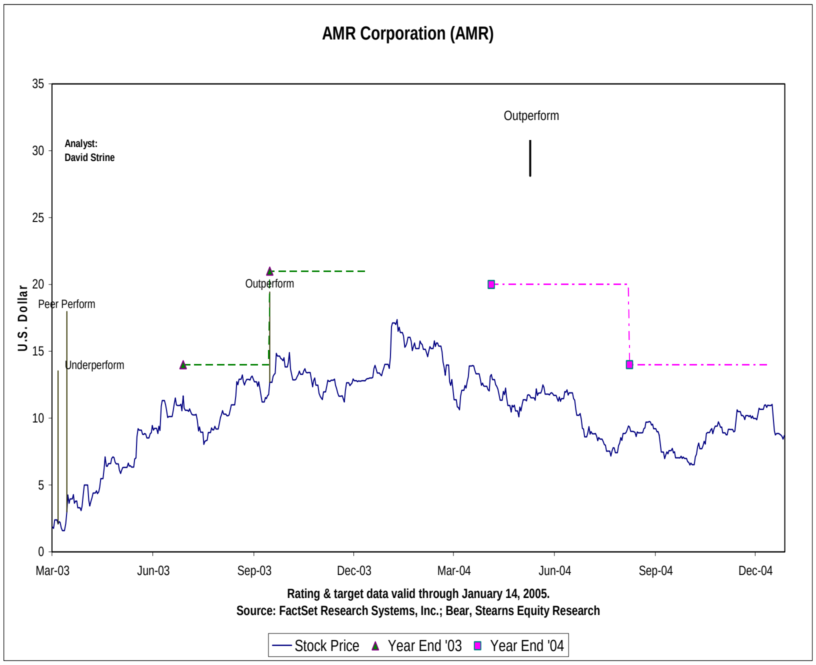
Source: Bear, Stearns & Co. Inc. estimates; company reports; company guidance.

Subject companies under coverage mentioned in this report:
Sector Rating — Market Weight

Alaska Air Group (ALK-29; Outperform)
AMR Corp. (AMR-8.97; Peer Perform)
Continental Airlines (CAL-12; Peer Perform)
Delta Air Lines (DAL-4.33; Peer Perform)
Northwest Airlines (NWAC-6.98; Outperform)

Addendum

Important Disclosures



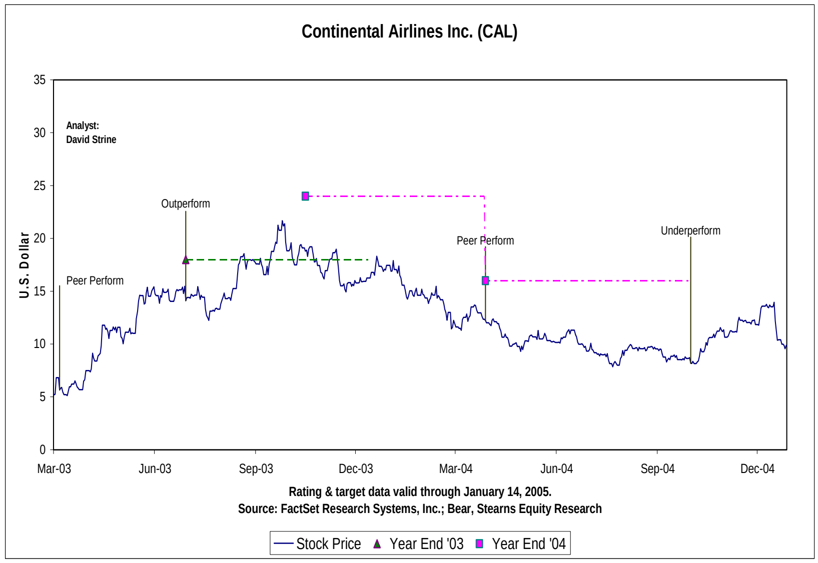
BSC Recommendation History since March 19, 2003 for:

AMR Corporation (AMR) - U.S. Dollar

Date	Stock Price	Rating	Target
**Analyst: David Strine			
24-Mar-03	2.38	UNDERPERFORM	---
01-Apr-03	2.10	PEER PERFORM	---
16-Jul-03	10.56	PEER PERFORM	14.00
03-Oct-03	11.75	OUTPERFORM	21.00
22-Apr-04	13.12	OUTPERFORM	20.00
26-Aug-04	9.42	OUTPERFORM	14.00
20-Oct-04	6.49	PEER PERFORM	---

Addendum

Important Disclosures

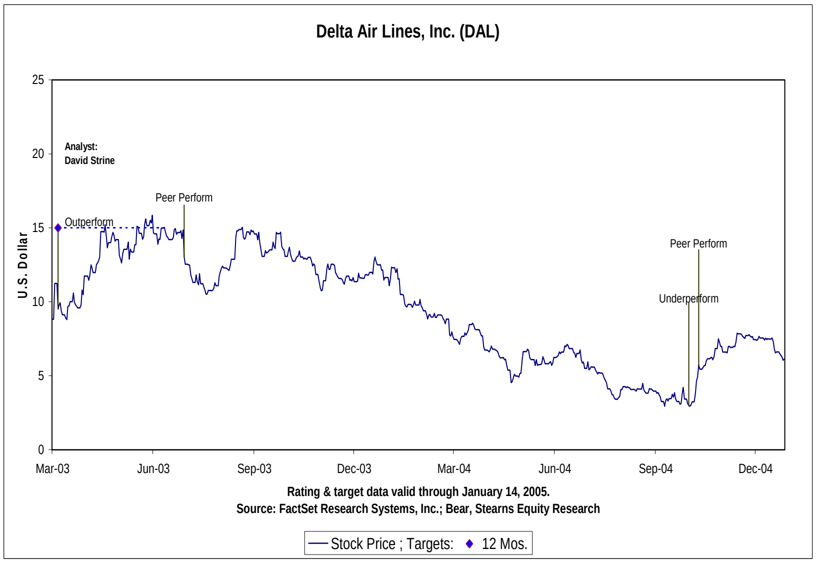


BSC Recommendation History since March 19, 2003 for:
Continental Airlines Inc. (CAL) - U.S. Dollar

Date	Stock Price	Rating	Target
**Analyst: David Strine			
24-Mar-03	6.82	PEER PERFORM	---
17-Jul-03	15.47	OUTPERFORM	18.00
03-Nov-03	19.10	OUTPERFORM	24.00
15-Apr-04	12.36	PEER PERFORM	---
19-Oct-04	8.71	UNDERPERFORM	---
25-Jan-05	9.51	PEER PERFORM	---

Addendum

Important Disclosures

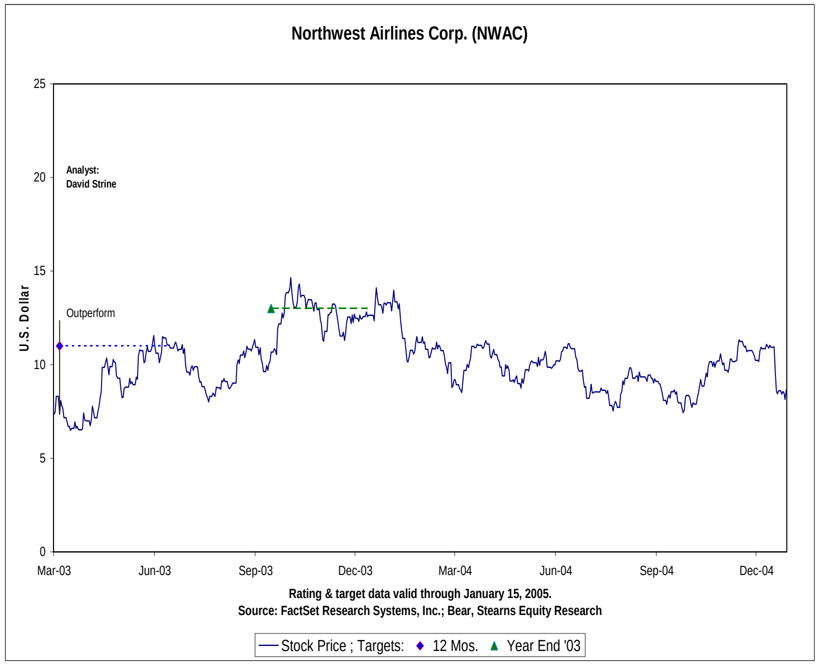


BSC Recommendation History since March 19, 2003 for:
Delta Air Lines, Inc. (DAL) - U.S. Dollar

Date	Stock Price	Rating	Target
**Analyst: David Strine			
24-Mar-03	11.25	OUTPERFORM	15.00
17-Jul-03	14.85	PEER PERFORM	15.00
19-Oct-04	3.11	UNDERPERFORM	---
28-Oct-04	4.94	PEER PERFORM	---

Addendum

Important Disclosures



BSC Recommendation History since March 19, 2003 for:
Northwest Airlines Corp. (NWAC) - U.S. Dollar

Date	Stock Price	Rating	Target
**Analyst: David Strine			
24-Mar-03	8.30	OUTPERFORM	11.00
03-Oct-03	10.16	OUTPERFORM	13.00
10-Mar-05	7.10	OUTPERFORM	11.00

Addendum

Important Disclosures

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Peer Perform (P) — Stock is projected to perform approximately in line with analyst's industry coverage universe over the next 12 months.

Underperform (U) — Stock is projected to underperform analyst's industry coverage universe over the next 12 months.

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David Strine

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